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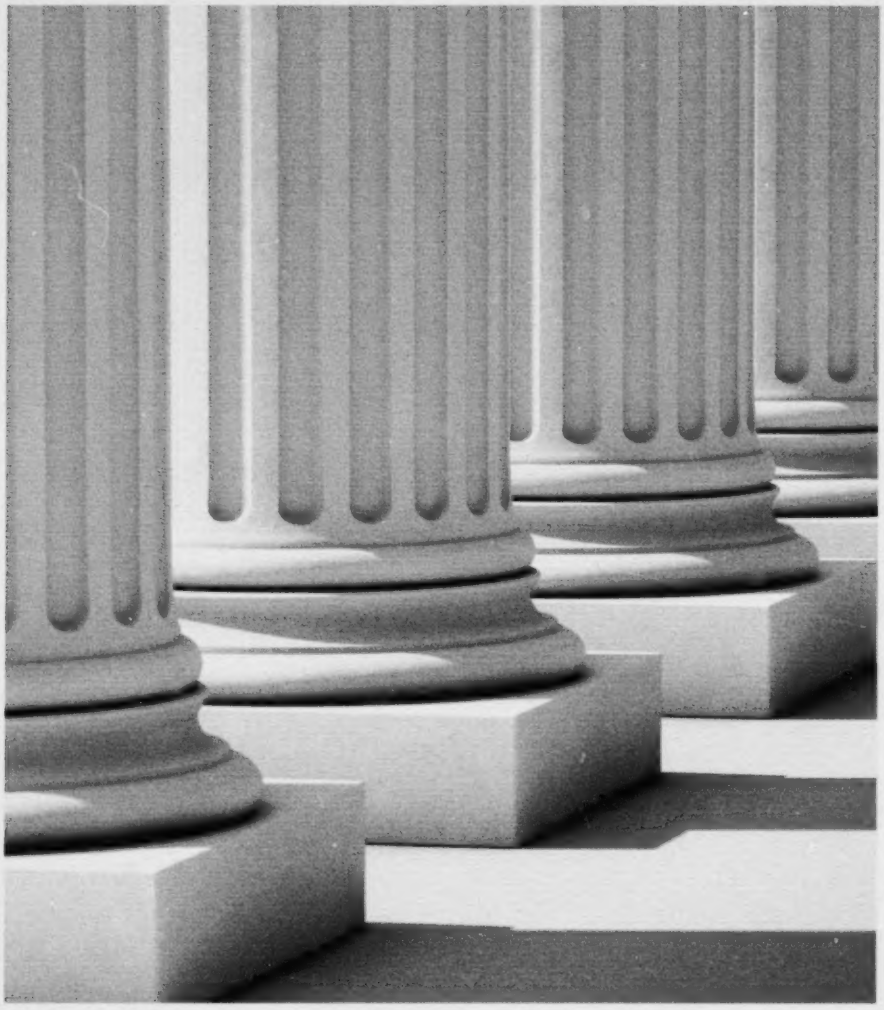

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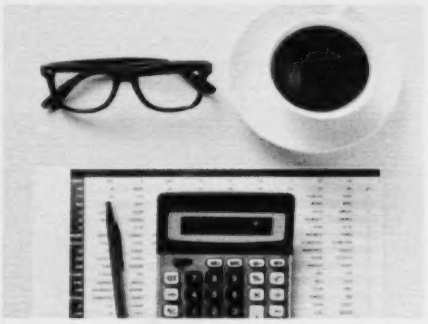

REVIEWABLE TRANSACTIONS

FINAL REPORT **108**

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UPDATES:

New Brunswick has adopted the Uniform Act as *Debtor Transactions Act*, SNB 2015, c 23.

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Alberta Law Reform Institute

The Alberta Law Reform Institute (ALRI) was established on November 15, 1967 by the Government of Alberta, the University of Alberta and the Law Society of Alberta for the purposes, among others, of conducting legal research and recommending reforms in the law. Funding for ALRI's operations is provided by the Alberta Law Foundation, the Government of Alberta, and the University of Alberta.

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This report is based on a uniform act prepared by the Uniform Law Conference of Canada [ULCC]. We are grateful for all of the work and analysis provided by the working group on that project and by delegates to the annual meeting who reviewed both the policy and the draft legislation.

Before a uniform act can be implemented, it must be custom fit into the specific provincial context. This report does precisely that. Initial carriage of this project was taken on by Maria Lavelle. ALRI was later fortunate to engage Professor Tamara Buckwold, who was the chair and leader of the ULCC working group, recognised expert and teacher in commercial law, and who is the primary author of this report. Her familiarity with the subject and the balancing judgments made by the working group were of considerable assistance to the Institute Board. We thank her for her analysis, exposition and articulation of modernised policies in this area.

Peter Lown provided assistance on the section on choice of law. Drafting of specific Alberta provisions was done by Sandra Petersson. Preparation of the report for publication was carried out by Ilze Hobin and Jenny Koziar.

We would also like to acknowledge the Law Reform Commission of Saskatchewan for their support of the ULCC project.

As always, the proposals are those of the Board as a whole. It is our hope that this antiquated and uncertain area of the law can be clarified and modernised very quickly.

Summary

The law of fraudulent conveyances and fraudulent preferences is part of the broader commercial law of creditors' remedies. Provincial fraudulent conveyances and fraudulent preferences law supports the civil enforcement regime by offering a remedy to creditors whose rights are subverted as a result of transactions that remove property of their debtors from the reach of judgment enforcement law. Corresponding provisions in the federal *Bankruptcy and Insolvency Act* allow a trustee in bankruptcy to recover property lost to creditors who are entitled to share in a distribution under the rules of that Act once bankruptcy proceedings are invoked. While those provisions are designed to serve the same purpose as that served by provincial law, the conditions under which a transaction may be set aside under the *Bankruptcy and Insolvency Act* differ from those that apply under provincial law. A trustee may rely on either regime but, outside of bankruptcy, creditors are restricted to provincial law.

Alberta law in this area, like the law in other Canadian common law provinces and territories, is seriously dated, lacks a clear policy foundation and produces anomalous and uncertain results. The widely acknowledged need for reform prompted the Uniform Law Conference of Canada [ULCC] to undertake a comprehensive project culminating in 2012 with its approval of the *Uniform Reviewable Transactions Act* [URTA], recommended by the Conference for adoption across the country. The Act is accompanied by a detailed commentary explaining the meaning and operation of its provisions. The central recommendation of this report is that the URTA be enacted in Alberta, with such minor revisions as may be appropriate to interface with other legislation and generally meet local legal requirements. The ancillary recommendations deal with those revisions.

This report does not review every provision of the URTA. It discusses the rationale for reform, the policy implemented by the Act and its primary features. Readers are directed for further detail to the Act and commentary, included as an Appendix. Footnote references identify additional source materials leading to ULCC approval of the URTA.

Chapter 1 – Introduction

This chapter explains the purpose of the law of fraudulent conveyances and fraudulent preferences, including its relationship with the provincial law of judgment enforcement and the federal law of bankruptcy. Judgment enforcement in Alberta is governed by the *Civil Enforcement Act* [CEA] and regulations. Fundamentally, fraudulent conveyances law is intended to protect the right of unsecured creditors to enforce their claims through seizure of the debtor's property under the judgment enforcement regime. Property transferred by a debtor to a third party and thereby put beyond

reach of enforcement measures may be recovered by creditors under prescribed circumstances. Fraudulent preferences law is intended to protect the right of unsecured creditors to share in the fruits of enforcement action taken against a debtor under the distribution scheme prescribed by the CEA. It allows unpaid creditors to recover property transferred by a debtor to one creditor in order to bring that property within the statutory sharing rules. Since judgment debt is unsecured, fraudulent conveyances law and fraudulent preferences law buttress the rights of recovery flowing from a money judgment granted on any cause of action.

This chapter also describes the comprehensive process that led to the drafting and approval of the URTA, and highlights the leadership role taken by Alberta in reforming judgment enforcement law through enactment of the CEA, which largely followed the ALRI's Report on *Enforcement of Money Judgments* (1991).

Chapter 2 – The Case for Reform

This chapter expands on the rationale for and importance of the law of fraudulent conveyances and fraudulent preferences. It outlines the sources and history of current law, highlighting the fact that the English *Fraudulent Conveyances Act, 1571* remains in effect today. It identifies, in general terms, the problems with current law and advances the case for resolution of those problems through reform. New legislation is required to bring clarity and certainty to this area of law through rules grounded in defensible and consistent policy. Reform would also complement the advances made through enactment of the CEA and the *Personal Property Security Act*, completing a modern and integrated statutory system of law governing creditors' rights. Reform through enactment of the URTA would potentially advance the harmonization of provincial law by inspiring corresponding reform in other jurisdictions.

Chapter 3 – Concepts in Reformed Legislation

Terminology and General Content

This chapter begins with an explanation of the terminology used in the URTA and its relationship to the terminology of existing law. The generic term "reviewable transaction" appears in the title to the Act and refers generally to the kinds of transactions that interfere with creditors' rights under circumstances that justify an order for relief. Transactions that deplete the pool of assets available to satisfy a judgment in the sense now described as fraudulent conveyances are differentiated from those that disrupt a creditor's right to be paid according to a statutory scheme of distribution, now described as fraudulent preferences. Since relief under the URTA is based in most cases on the effect of a transaction rather than the intention of its participants, the word "fraudulent" is abandoned as a descriptor. Under the

URTA, the type of case involving interference with creditors' rights of enforcement now called a "fraudulent conveyance" is simply a "transaction" falling within the Part 2 of the Act, which applies to transactions at undervalue and transactions intended to defeat creditors. A preferential payment of the kind now called a "fraudulent preference" is a "creditor transaction" falling within Part 3. Any form of transaction is "reviewable" where the specified grounds for relief exist.

The rest of the chapter is devoted to a review of the primary features of the URTA and the policies on which it is based. An attempt to summarize the discussion relating to each of those features here would be unhelpfully duplicative of the main text. However, three essential themes are worthy of special note.

Balancing Competing Interests: The Central Policies

A reviewable transaction involves a transfer of property or value by a debtor to another person, who is called the "transferee" both descriptively and in the language of the statute. Where the transfer depletes the debtor's asset base such that it is insufficient to satisfy the claims of creditors, they may seek to recover from the transferee the value received from the debtor. This sets up a zero sum game in which both creditors and transferees are claiming the same property or equivalent value; a gain to one represents a corresponding loss to the other. The Act is therefore designed to balance the right of creditors to recover what they are owed against the right of a transferee to be free of unsuspected claims to property or value received from a person who has creditors. The Act employs a combination of strategies to balance the interests of creditors and transferees. These strategies include, among others, the design of the grounds on which creditors may claim relief against a transferee and the provisions defining the nature of the order for relief that may be granted.

The Grounds for Relief

The report discusses the grounds for relief that apply to the two transactional patterns described above; namely, transactions at undervalue and transactions intended to defeat creditors, governed by Part 2, and creditor transactions, governed by Part 3. The main point to be made here is that in both cases the primary basis for relief to creditors is the effect of a transaction in impeding their rights of enforcement or their right to share. Creditors must prove facts demonstrating that a transaction had the effect of undermining creditors' rights, a condition that is met by proof of the debtor's insolvency. In such a case, creditors need not prove that the debtor intended to defeat their claims. Notably, creditors are entitled to relief only when the circumstances are such that the transferee was in a position to recognize the risk that the transaction might be subject to challenge. The policy of protecting creditors' rights is accordingly balanced with the policy of

protecting the reasonable expectations of transferees and preserving the finality of transactions. Since the existence of grounds for relief may be determined on objective grounds without inquiry into the debtor's state of mind, the likely outcome of potential litigation may be predicted with reasonable accuracy. The risk of a transaction may be assessed by prospective participants, creditors and transferees may be given useful advice by their legal counsel and courts may reach principled and consistent decisions. The elimination of proof that the debtor intended to defeat creditors as a requirement under the primary grounds for relief constitutes one of the most significant progressive changes in the proposed legislation. While Part 2 of the Act includes secondary grounds for relief that are intention-based, creditors are likely to rely on those grounds in relatively few cases.

The three grounds for relief in a Part 2 case may be summarized as follows:

1. The debtor was insolvent or imminently insolvent at the time of the transaction and the transferee gave no consideration for value received from the debtor or gave "conspicuously less" than reciprocal value (section 7(1)(a)).

2. The debtor intended to and did impede creditors' rights of enforcement by means of the transaction and the transferee gave no consideration for value received from the debtor or gave "conspicuously less" than reciprocal value (section 7(1)(b)).

3. The debtor and transferee jointly intended to and did impede creditors' rights of enforcement by means of the transaction (section 7(1)(c)).

In all three cases, the effect of the transaction is to impede or defeat creditors' rights of recovery and the transferee is in a position to recognize that the transaction is vulnerable, either because its terms are conspicuously too good to be true or because he or she knows of and intends to facilitate the debtor's intention to obstruct creditors.

In a Part 3 case, relief is available where the debtor was insolvent or imminently insolvent at the time the transferee creditor was paid and the paid creditor was not at arm's length from the debtor. Here, the effect of the payment is to impede creditors' rights to share because the debtor is insolvent and incapable of satisfying all of their claims, and the relationship between the transferee creditor and the debtor is such that the transferee is in a position to recognize the risk that the payment may be subject to challenge.

The Order for Relief

If a transaction is successfully challenged under current law, the transaction is "void" under the applicable statute. The problems of interpretation and result presented by this approach are overcome under the URTA by the nuanced and comprehensive rules governing the order for relief. In the case of a Part 2 transaction, the court is directed to make available to the applicant creditor the value conferred on the transferee under the transaction to the extent of the applicant's claim, taking into account identified qualifying factors. Those factors include any consideration that may have been given by the transferee. The result is to restore to the applicant creditor the value lost through the transaction while the transferee loses only the value for which payment was not given. In the case of a Part 3 creditor transaction, the court is directed to make an order that effectively sets aside the transaction, reversing the payment and consequently channeling the amount received by the paid creditor into the creditor sharing scheme. A number of supplementary provisions address the terms of the order in further detail.

Other Matters

Chapter 3 discusses a number of more specific issues addressed by the URTA. In each case, the Act is designed to overcome a point of uncertainty in current law, to implement a better approach or to establish a rule where no rule exists. The issues addressed in the report include the grounds for relief in special cases falling within Part 2, standing to seek relief, transactions involving exempt property, limitation of actions, choice of law, the position of secured creditors and recovery against secondary transferees. Additional matters of a largely technical nature addressed by the URTA are not canvassed in the report.

Chapter 4 – Implementing the Uniform Reviewable Transactions Act in Alberta

This chapter discusses the details of enacting the URTA in Alberta. A few minor changes in wording are suggested to enhance the clarity of the Act. The remaining points of discussion are addressed to integration of the URTA with existing legislation and with the personal property and land registry systems. These points of detail are covered in the recommendations advanced.

Recommendations

RECOMMENDATION 1

The Uniform Reviewable Transactions Act should be enacted in Alberta with minor revisions as may be required to: incorporate the changes in the Recommendations in this Report, appropriately cross-reference Alberta legislation and conform to local drafting protocols.....47

RECOMMENDATION 2

Section 3 of the Uniform Reviewable Transactions Act should be revised to make it clear that a secured creditor has standing to apply for relief and that the order for relief granted to a secured creditor is limited to the amount of the claim that is unsecured (i.e., specifically, the amount that exceeds the value of the property against which the claim may be enforced).....50

RECOMMENDATION 3

Section 18 of the Uniform Reviewable Transaction Act should refer to the *Civil Enforcement Act* and be expanded to provide more explicit direction as to how the stated objective should be achieved through a non-exhaustive listing of potential types of order. 52

RECOMMENDATION 4

Section 20 of the Uniform Reviewable Transactions Act should be revised to provide that a court may grant an attachment order that may be registered against a transferee or against land affected by the order where the transaction to which the order relates involves exempt property that the debtor continues to use in a manner that attracts the exemption, and should also clarify how the *Civil Enforcement Act* operates in relation to that order.....54

RECOMMENDATION 5

Section 23 should be amended to authorize the court to issue an attachment order in addition to or as an alternative to an injunction; an attachment order issued under this section should be subject to the provisions of the Civil Enforcement Act governing attachment orders generally 56

Table of Abbreviations

LEGISLATION

ABCA	*Business Corporations Act*, RSA 2000, c B-9
BIA	*Bankruptcy and Insolvency Act*, RSC 1985, c B-3
CEA	*Civil Enforcement Act*, RSA 2000, c C-15
PPSA	*Personal Property Security Act*, RSA 2000, c P-7
URTA	*Uniform Reviewable Transactions Act*, online at: Uniform Law Conference of Canada <www.ulcc.ca/en/uniform-acts-new-order/current-uniform-acts/615-josetta-1-en-gb/uniform-actsa/reviewable-transactions-act/1390-uniform-reviewable-transactions-act-2012>

OTHER PUBLICATIONS

Dunlop & Buckwold	CRB Dunlop and Tamara M Buckwold, *Debt Recovery in Alberta* (Toronto: Carswell 2012)

CHAPTER 1

Introduction

[1] The law of fraudulent conveyances is often merged with the law of fraudulent preferences under the joint title "fraudulent conveyances and preferences law". The two bodies of law are distinct but linked by a central commonality. Both are adjuncts to the law of judgment enforcement and both respond to dealings with property that interfere with the rights of creditors realized through judgment enforcement measures.

[2] Judgment enforcement law is the means by which unsecured debt of any kind is satisfied if not voluntarily paid. The term "unsecured debt" sometimes refers to a financial obligation arising from a transaction of borrowing or credit in which the debtor has not given security for payment, but it has a broader meaning as used here and generally in this report. A judgment debt is itself unsecured, so "unsecured debt" is debt arising from a money judgment or potential judgment, including a judgment to recover unsecured debt in the narrower sense of an unpaid financial obligation. This underscores the importance of an effective system of judgment enforcement law; it is the means by which monetized claims arising from any cause of action are recovered. Judgment enforcement law, represented in Alberta primarily by the *Civil Enforcement Act*,[1] allows a judgment creditor to seek satisfaction through seizure of the judgment debtor's assets or income through prescribed measures.[2] Since judgment enforcement entails recourse against the debtor's property, creditors' rights are prejudiced if the debtor transfers away property or otherwise gives value in a manner that materially diminishes the pool of assets against which creditors can seek satisfaction. Fraudulent conveyances law and fraudulent preferences law, respectively, allow creditors to challenge such a transaction under prescribed circumstances.

[3] Fraudulent conveyances law is designed to protect creditors generally. It comes into play when a debtor transfers away property, diminishing his or her

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[1] *Civil Enforcement Act*, RSA 2000, c C-15 [CEA].

[2] The word "seizure" is used here in the generic sense of steps taken under the CEA to liquidate assets or channel them into the hands of judgment creditors in the manner appropriate to the type of property in question; seizure as a formal procedural step is not always required. The regular processes authorized by the CEA include seizure and sale of personal property, sale of land without the preliminary requirement of seizure or garnishment of monetary obligations such as bank accounts, financial investments and employment earnings.

asset base and curtailing enforcement of existing or prospective judgments commensurately. In effect, the transferee is forced to disgorge the property received in favour of the transferor's creditors. Fraudulent preferences law deals with a transfer of property to pay one of a number of creditors, where the result of the transfer is to reduce the debtor's asset base such that others cannot recover at all or to the same extent as the creditor who was paid. The "preferred" creditor is forced to share the property taken in payment according to a proportional satisfaction regime imposed by law.

[4] Since the law governing creditors' rights of recovery is primarily a matter of property and civil rights falling within the jurisdiction of the provinces and territories, fraudulent conveyances and fraudulent preferences are governed primarily by provincial law. Provincial law overlaps with federal law when a debtor becomes subject to bankruptcy or insolvency proceedings under the federal *Bankruptcy and Insolvency Act* [BIA].[3] Although the BIA employs different terminology, it includes rules under which transactions that might be described in traditional terms as fraudulent conveyances and fraudulent preferences may be challenged. In 2006, the Uniform Law Conference of Canada [ULCC] approved a project for reform of the provincial and territorial law of fraudulent conveyances and fraudulent preferences.[4] The project did not directly address federal law, though the existence and content of the BIA provisions were taken into account in the development of recommendations for reform.

[5] The ULCC project was launched by two comprehensive study papers delivered in 2007 and 2008 respectively, one addressing each of the two areas.[5] The study papers outlined the current law, identified the issues to be resolved through potential reform and canvassed solutions offered by the legislation of other jurisdictions, previous law reform reports and academic commentary. A

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[3] *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 [BIA]. A trustee in bankruptcy may challenge a transaction both under the BIA and under provincial law. See *Robinson v Countrywide Factors Ltd*, [1978] 1 SCR 753.

[4] The project was facilitated by funding from the Saskatchewan Law Reform Commission. All of the documents submitted to the ULCC and noted in this report are available in English on the website of the Saskatchewan Commission. Pursuant to the bijural policy of the ULCC, only those that were translated into French are available on the ULCC website in either language. Since the reports were numerous and in some instances lengthy, some were not translated.

[5] Tamara M Buckwold, "Reform of Fraudulent Conveyances and Fraudulent Preferences Law (Transactions at Undervalue and Preferential Transfers), Introduction and Part I: Transactions at Undervalue" (2007), online at: Uniform Law Conference of Canada <www.ulcc.ca/en/2007-charlottetown-pe/216-civil-section-documents/582-reform-of-fraudulent-conveyances-and-preferences-law-introduction-and-part-i-2007>; Tamara M Buckwold, "Reform of Fraudulent Conveyances and Fraudulent Preferences Law (Transactions at Undervalue and Preferential Transfers), Part II: Preferential Transfers (2008), online at: Uniform Law Conference of Canada <www.ulcc.ca/images/stories/2008_en_pdfs/2008ulcc0010.pdf>.

working group was then constituted to develop recommendations for a uniform statute.[6] The group comprised academics, government lawyers and practitioners from across Canada. It produced a series of extensive reports proposing recommendations that were adopted by the ULCC in successive years.[7] The recommendations were incorporated in the *Uniform Reviewable Transactions Act* [URTA] with Commentary, adopted by the Conference in 2012.[8]

[6] The URTA deals separately with the types of case that currently fall within the rubric of fraudulent conveyances and fraudulent preferences, respectively. The two branches of the Act are linked by a common underlying policy and intersect through a common definitional structure, as well as some shared provisions. The name of the statute signals the fact that it applies to a range of transactions that are subject to review on the grounds that they interfere with creditors' rights and reflects the nomenclature commonly used today in relation to this area of law.

[7] Alberta led the reform of provincial and territorial judgment enforcement law with the enactment in 1994 of the CEA. The Act substantially followed the recommendations and draft Judgment Enforcement Act proposed by the Alberta Law Reform Institute and has been influential in the subsequent reform of judgment enforcement law elsewhere in Canada. [9] Alberta now has the opportunity to advance that leadership role by reforming the supplementary law

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[6] Professor Tamara M Buckwold of the Faculty of Law at the University of Alberta was Chair of the ULCC working group and is the primary author of this report.

[7] The recommendations developed by the working group were produced on the basis of 29 discussion papers reviewed in the course of 23 recorded meetings, on file with the Chair. Minutes of the meetings were kept by Thomas Anderson, QC of Vancouver. The recommendations adopted by the ULCC were advanced in the following reports:

- Reform of Fraudulent Conveyances and Fraudulent Preferences Law (Transactions at Undervalue and Preferential Transfers), Part 1: Transactions at Undervalue & Fraudulent Transactions, Final Report of the Working Group (Halifax 2010), online: Uniform Law Conference of Canada <www.ulcc.ca/images/stories/2010_pdf_en/2010ulcc0032_Fraudulent_Conveyances_Transactions_Undervalue_Final_Report.pdf>;
- Reform of Fraudulent Conveyances and Fraudulent Preferences Law (Transactions at Undervalue and Preferential Transfers), Part 1: Transactions at Undervalue & Fraudulent Transactions, Supplementary Report of the Working Group (Winnipeg 2011) and Reform of Fraudulent Conveyances and Fraudulent Preferences Law, Part 2: Preferential Transfers, Final Report of the Working Group (Winnipeg 2011), online: Uniform Law Conference of Canada <www.ulcc.ca/images/stories/2011_pdf_en/2011ulcc0005.pdf>.

[8] See Appendix A.

[9] Alberta Law Reform Institute, *Enforcement of Money Judgments*, Vols 1 & 2, Report No 61 (1991). The reformed system departs from ALRI's recommendations primarily in the privatization of functions previously performed by the civil service Sheriff through the designation of formally authorized civil enforcement agencies, who act under the supervision of the Sheriff – Civil Enforcement.

of fraudulent conveyances and fraudulent preferences. Fortunately, most of the work required to achieve reform has been done through the comprehensive process culminating in the URTA. Its drafters were cognizant of the need to interface the proposed statute with modern judgment enforcement legislation and the Act could be enacted in Alberta with the limited revision required to accommodate provincial drafting protocols, ensure a proper linkage with provincial legislation and implement incidental policy choices on a few points of detail. An Alberta version of the uniform Act would both accomplish the much-needed reform of Alberta law and set a precedent that may inspire the harmonization of provincial and territorial law across the country.

CHAPTER 2

The Case for Reform

A. Introduction

[8] The role of fraudulent conveyances and fraudulent preferences law in supplementing the law of judgment enforcement was described in the introduction. Judgment enforcement is the only means by which unsecured debt that is not voluntarily paid may be recovered short of bankruptcy or insolvency proceedings under federal legislation. Judgment enforcement law is the "clout" behind a money judgment granted on any cause of action, and judgments for the payment of money are by far the most common judicial remedy. This is the law that gives effect to rights of compensation for loss or injury associated not only with debt produced by borrowing or credit, but with accidental or intentional injury to person or property, the non-fulfilment of family responsibilities, environmental violations, breach of contract, breach of fiduciary obligations or any of the myriad legal doctrines that impact the lives of citizens and the functioning of the economy. Subject to the limited shelter of exemptions legislation, the property of a judgment debtor who fails to pay the amount of a judgment is the sole source of satisfaction.

[9] The law of fraudulent conveyances and fraudulent preferences is intended to safeguard the rights of judgment creditors by allowing them to recover property that would otherwise be lost through the actions of their debtors. Unfortunately, its deficiencies are such that the expectation is frequently unfulfilled. Current law is complex, antiquated and ambiguous, producing results that are often unpredictable and sometimes indefensible. These are not desirable features in a system of law that significantly impacts the ability of creditors to recover claims validated by judgment. Perversely, the very fact that this law is technically difficult and poorly understood has impeded reform in spite of repeated criticism and the attempts of other law reform bodies to address its deficiencies. [10]

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[10] In addition to the reports produced in the ULCC project, see Karl Dore and Robert Kerr, *Third Report of the Consumer Protection Project: Legal Remedies of the Unsecured Creditor after Judgment* (Fredericton: Government of New Brunswick, 1976); Ontario Law Reform Commission, *Report on the Enforcement of Judgment Debts and Related Matters*, vol 4 (1983) at 125-245; Law Reform Commission of British Columbia, *Report on Fraudulent Conveyances and Fraudulent Preferences, LRC 94* (1988).

B. Fraudulent Conveyances

[10] The rationale for provincial fraudulent conveyances law is obvious. A debtor should not be permitted to defeat the legal rights of creditors by the simple expedient of transferring away property that could otherwise be reached through judgment enforcement measures to satisfy their claims – a practice often referred to as "judgment proofing". English judges and legislators responded early on to the problem, and Canadian legislators and courts have further contributed to the body of principles comprising the law in this area.

[11] The current law governing fraudulent conveyances draws from three sources. Remarkably enough, the first is the English *Fraudulent Conveyances Act, 1571*, which remains in effect as received Alberta law and is the primary basis upon which litigation challenging transfers of property that defeat creditors' claims proceeds. [11] Secondly, the *Fraudulent Preferences Act* includes rules distinct from but overlapping with those of the *Fraudulent Conveyances Act, 1571*, under which a transfer of property that defeats creditors' rights but is not a preferential payment may be avoided. [12] The *Fraudulent Preferences Act* was first enacted in Alberta in 1922 and derived from provincial legislation enacted earlier in the century. It has remained relatively unchanged since. The third source of law lies in the centuries-long accumulation of judicial decisions interpreting and applying the two statutory enactments.

[12] In the service of interpretation, the courts have engrafted on the wording of the statutes requirements and presumptions that are not at all evident on their face, adding to rather than resolving the uncertainty resulting from the gaps, inconsistencies and anomalies in the legislation itself. It has been said in reference to the case law interpreting the *Fraudulent Conveyances Act, 1571* that, "The result is a common law gloss which comes close to erasing the Act itself." [13] The picture is further complicated by the fact that the conditions of relief under the *Fraudulent Conveyances Act, 1571* are similar in some respects to those of the *Fraudulent Preferences Act* but differ in others so a challenge that might not meet

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[11] More fulsomely and properly titled the *Act Against Fraudulent Deeds, Gifts, Alienations, etc.* (UK), 13 Eliz 1, c 5, often called the *Statute of Elizabeth*. The Act is also in effect in most other provinces, either as received law or through statutory re-enactment.

[12] *Fraudulent Preferences Act*, RSA 2000, c F-24.

[13] CRB Dunlop and Tamara M Buckwold, *Debt Recovery in Alberta* (Toronto: Carswell 2012) at 959 [Dunlop & Buckwold]. To similar effect see Law Reform Commission of British Columbia, *Report on Fraudulent Conveyances and Fraudulent Preferences, LRC 94* (1988) at 8: "The law only becomes baffling when one considers the 400 odd years of jurisprudence surrounding this legislation."

the requirements of the latter may succeed under the former and, less often, *vice versa*. As a result, confusion prevails over the rules, principles and judicial authorities that govern the outcome in any given case. A decision directed to an action under one statute may be authoritative in relation to the similar provision of the other, but qualified by the differences between them.

C. Fraudulent Preferences

[13] As its name implies, the *Fraudulent Preferences Act* is addressed primarily to the preferential payment of creditors and, supplemented by the case law, is the source of provincial law on that subject. The existence and continuing need for provincial fraudulent preferences legislation requires explanation.

[14] Fraudulent preferences legislation proceeds on the principle that unsecured creditors who are not voluntarily paid by a common debtor are entitled to recover *pari passu* against the debtor's assets. This principle is realized most fully in bankruptcy law, under which a bankrupt debtor's trustee in bankruptcy is required to distribute the bankruptcy estate remaining after satisfaction of secured and preferred creditors *pro rata* among unsecured creditors who have proven their claims. The creditor sharing principle was incorporated in 19th century Dominion bankruptcy legislation enacted under the federal government's constitutional jurisdiction over bankruptcy and insolvency. The federal *Bankruptcy Act* was repealed in 1880 and not replaced until a new Act was passed in 1919. In the interstitial period, provincial legislators enacted a package of legislation designed to facilitate collective recovery by creditors through a system comparable to that ordinarily implemented through bankruptcy law. The statutory rules that provided for proportionate sharing among creditors who took enforcement action came to be known generally as creditors' relief legislation. Like bankruptcy legislation, the provincial statutes also included rules designed to prevent creditors from circumventing the principle of equitable sharing by taking payments from an insolvent debtor that would "prefer" the creditor so paid by leaving insufficient assets to satisfy the debts owed to others.

[15] The federal government reasserted its constitutional jurisdiction over bankruptcy and insolvency with the proclamation of the 1919 *Bankruptcy Act* but many provinces, including Alberta, retained a modified version of the creditor sharing principle in their judgment enforcement systems, along with anti-

preference legislation designed to protect that principle.[14] The creditor sharing principle as manifested in provincial law required judgment creditors who took enforcement measures through execution to share the proceeds *pari passu* with other unsecured creditors who had filed with the sheriff a writ of execution or a certificate proving a liquidated debt.[15] The concept is now embodied in the distribution rules in Part 11 of the CEA, though in qualified form. Only creditors who have obtained judgment and registered a writ of enforcement are entitled to share in a distribution, and the "instructing creditor" who has initiated enforcement action receives a bonus payment in recognition of the effort and financial investment involved in the proceedings. The anti-preference rules of the early 20th century remain in effect and largely unchanged in the *Fraudulent Preferences Act*. The important point here is that the sole rationale for provincial anti-preference legislation is the existence of provincial law that entitles unsecured creditors to share in the assets of a joint debtor through a legally prescribed scheme. Without the creditor sharing rules of the CEA, there would be no justification for provincial anti-preference law.[16] Debtors would be entitled to pay creditors as they wish and creditors would have no legal grounds for complaint.

[16] While provincial fraudulent preferences law is comparatively less ancient and obscure than the law of fraudulent conveyances, existing legislation lacks a clear interface with the creditors' relief legislation it is intended to support, is ambiguous in its terms, limited in scope and largely ineffective.

D. Conclusion

[17] This brief account of the history and sources of law exemplifies the need for modern legislation implementing coherent policies and clear principles designed to produce appropriate and predictable outcomes for both creditors

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[14] Retention of the creditor sharing principle in provincial judgment enforcement law makes the Canadian common law jurisdictions unique among jurisdictions that otherwise share our English legal heritage. At common law, judgment creditors are entitled to satisfaction on a first-in-time basis; a creditor who takes steps to enforce a judgment is not obliged to share with others, regardless of whether they remain unpaid. Any claim to share proportionately can be realized only through the invocation of bankruptcy proceedings.

[15] The creditor sharing rules were retained in the *Execution Creditors Act*, RSA 1980, c E-14, repealed with the enactment of the CEA.

[16] The history of Alberta legislation is detailed by the Alberta Law Reform Institute, *Enforcement of Money Judgments*, Vol 1, Report No 61 (1991) at 326 - 29. The Institute report discusses whether the creditor sharing principle should be retained in the proposed reform of judgment enforcement law and addresses the scope and implementation of that principle (at 329 *et seq*).

and debtors. Law based on legislation enacted 100 years ago, in the case of fraudulent preferences, and 450 years ago, in the case of fraudulent conveyances, is overdue for systematic reform. This assessment of the current law, offered in the paper that prompted the ULCC to launch its project, is pertinent: [17]

> Texts and essays on the law are full of criticism of confused rules, redundant statutory provisions, perplexing and contradictory decisions, antiquated rules and ideas, and opaque policy. Fraudulent conveyances and preferences problems have not produced far-reaching and imaginative judicial decisions. The vast majority of cases say little or nothing about the law, simply copying passages from leading decisions.

[18] The passage quoted underlines the primary deficiencies that should be addressed through statutory reform; lack of clarity in the rules and principles comprising the law and the absence of a clear and deliberate policy foundation informing it.

[19] There is another reason to engage reform in this area, and that is the need to integrate fraudulent conveyances and fraudulent preferences law into the modern and efficient system of law governing creditors' rights established through the reform of its other primary branches. The CEA modernized, clarified and rationalized the law governing recovery of unsecured debt through judgment enforcement, an area that previously suffered from many of the problems manifest in fraudulent conveyances and preferences law. The pre-reform law was described, in terms that could equally have been addressed to the law of fraudulent conveyances and preferences, as "a patchwork of English and Canadian legislation and judge-made rules which do not fit together into a comprehensible or workable pattern," and in "urgent need of reform."[18] The CEA drew much from the *Personal Property Security Act* [PPSA] enacted in 1988 to replace a fragmented and inefficient system of law governing the recovery of debt secured by an interest in personal property of the debtor. [19] The current law of fraudulent conveyances and fraudulent preferences is oblivious to the policies, concepts and procedures incorporated in these enormously successful statutes, a

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[17] CRB Dunlop, "Fraudulent Conveyances and Preferences: A Feasibility Study" (Paper presented to the Uniform Law Conference of Canada, August 23-26, 2004), online: Uniform Law Conference of Canada <www.ulcc.ca/en/2004-regina-sk/272-civil-section-documents/964-fraudulent-conveyances-and-preferences>.

[18] CRB Dunlop, *Creditor-Debtor Law in Canada*, 2nd ed (Toronto: Carswell 1995).

[19] *Personal Property Security Act*, RSA 2000, c P-7 [PPSA].

fact that further militates for its reform. The law in this area is an anachronism and an anomaly; the horse-and-buggy in the parking lot of creditor-debtor law.

[20] Finally, reform through enactment in Alberta of the URTA would advance the goal of harmonizing an important area of commercial law across Canada. There is reason to believe that leadership on this front would inspire legislative action elsewhere, as the enactment of the CEA did in relation to judgment enforcement law generally.[20]

[20] The Legislative Services Branch of the New Brunswick Office of the Attorney General has already expressed its interest in enacting the URTA in that province. See Law Reform Notes #36: December 2014 online: <www2.gnb.ca/content/dam/gnb/Departments/ag-pg/PDF/en/LawReform/Notes36.pdf>.

CHAPTER 3

Concepts in Reformed Legislation

A. Introduction

[21] This report surveys the central features of the Uniform Law Conference of Canada URTA. The primary provisions of the Act, the policies motivating them and their basic operation are reviewed in this chapter. The comprehensive section-by-section explanation provided in the commentary to the Act is not reproduced; readers are encouraged to consult the Act and commentary for further detail.

B. The Terminology

[22] Provincial law and legal commentary addressing transfers of property that undermine the rights of the transferor's creditors use the historically entrenched terminology of "fraudulent conveyances" and "fraudulent preferences". The language derives from the wording of the *Fraudulent Conveyances Act, 1571,* which elaborately and resoundingly condemns transfers,

> ...devised and contrived of Malice, Fraud, Covin, Collusion or Guile to the End, Purpose and Intent to delay, hinder or defraud Creditors and others of their just and lawful Actions, Suits, Debts, Accounts, Damages, Penalties, Forfeitures, Heriots, Mortuaries and Reliefs, not only to the Let or Hinderance of the due Course and Execution of Law and Justice, but also to the Overthrow of all true and plain Dealing, Bargaining and Chevisance between Man and Man, without the which no Common wealth or civil Society can be maintained or continued.

[23] The statute in its complete iteration both provides a civil remedy to creditors through avoidance of the transfer and imposes the penal sanctions of fine and imprisonment against the parties, but the penal provisions are not in effect in Alberta.[21] The continued use of the language of fraud reflects the central requirement of the grounds for civil recovery, namely, proof that the transferor-debtor intended in making the transfer to defeat, hinder or delay creditors. It has long been established that a transfer of property that will necessarily have an

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[21] *Connors v Egli,* [1924] 1 WWR 1050 (Alta CA). This is likely also the case in other provinces and territories in which the Statute otherwise remains in effect. See CRB Dunlop, *Creditor-Debtor Law in Canada,* 2nd ed (Toronto: Carswell 1995) at 595.

adverse effect on creditors can be set aside even though it might be intended to achieve a laudable goal, such as providing for family or supporting a charitable cause.[22] The word fraud and derivations thereof are therefore used in the quite diluted sense that relief is available when a debtor knows that a transfer of property will put the property beyond the reach of creditors, but not necessarily in the sense that the transfer is maliciously motivated or even knowingly wrong either legally or morally.

[24] Reformed legislation in other jurisdictions and the reforms that would be implemented under the URTA focus on the effect of a transaction in defeating creditors' rights as the basis for relief. The debtor's intention may be relevant in some contexts but proof of intention to interfere with creditors' rights is not always required and, when it is, the relevant intention is only "fraudulent" in the limited sense just described; terminology referring to a fraudulent conveyance or preference is accordingly misleading.[23] The generic term "reviewable transaction" is adopted in the title to the proposed legislation and is used in this report to refer generally to the kinds of transaction that interfere with creditors' rights, the elements of which may justify an order for relief under the URTA. Transactions that deplete the pool of assets available to satisfy a judgment in the sense now described as a fraudulent conveyance are differentiated from those that disrupt a creditor's right to be paid according to a *pro rata* or modified *pro rata* sharing scheme, now described as a fraudulent preference. Part II of the Act, dealing with the first type of case is titled "Transactions at Undervalue and Fraudulent Transactions" to signify that it applies both to transactions that have the effect of defeating creditors' rights through diminution of their debtor's asset base regardless of the debtor's intention and transactions that are "fraudulent" in the limited sense that they are intended to and do obstruct creditors by other

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[22] The judgment in the leading case of *Freeman v Pope* (1870), 18 WR 906, LR 5 Ch 538 is the source of the aphorism that "persons must be just before they are generous".

[23] Since the early 20th century, American state law has been modeled on uniform legislation that offers a remedy without proof that the debtor actively intended to defraud or otherwise defeat creditors' rights. The first iteration was the *Uniform Fraudulent Conveyance Act*, promulgated by the National Conference of Commissioners on Uniform State Laws in 1918. That Act remains in effect in two states but has otherwise been supplanted by the *Uniform Fraudulent Transfers Act*, approved by the Conference in 1984. In 2014, the Conference issued a slightly modified revision of the Act, retitled the *Uniform Voidable Transactions Act*. As explained in a recent article by Kenneth C. Kettering, Reporter for the 2014 Act, "The main purpose of the renaming is to replace the long-used but misleading word "fraudulent" with terminology that will not mislead." Kettering goes on to explain that "[F]raud, in the modern sense of that word, is not, and never has been, a necessary element of a claim for relief under the act. The misleading suggestion to the contrary in the act's original title has led to misunderstandings..." See "The Uniform Voidable Transactions Act; or, the 2014 Amendments to the Uniform Fraudulent Transfer Act" (December 21, 2014) at 29 - 30, Business Lawyer, forthcoming. Available at SSRN: http://ssrn.com/abstract=2541949.

means. A different subtitle is suggested later in this report, since the word "fraudulent" may be misleading if understood to indicate something more. The title "Transactions at Undervalue and Transactions Intended to Hinder or Defeat Creditors" would be wordier but more accurate. Part III of the Act deals with transactions that disrupt the *pro rata* creditor sharing scheme and is titled "Preferential Creditor Transactions".

[25] The defined word "transaction" is used throughout rather than conveyance, transfer or something to similar effect in recognition of the fact that the Act is not limited to transfers of property by a debtor but includes virtually any action that has the effect of conferring a benefit on another person in a way that reduces the value of the asset pool available to creditors.[24] For example, a transaction may be the assumption of an obligation or the provision of unremunerated or under-remunerated services by a debtor. The choice of "transaction" might be criticized on the grounds that it may be taken to imply reciprocal exchange between the debtor and the person benefited, while the Act also encompasses the conferral of value by a debtor with no recompense at all. However, no single word can capture the full scope of the Act. "Transaction" is suggested on the grounds that it most closely represents its subject.[25] The term "creditor transaction", also defined, differentiates a transaction that satisfies a debt in violation of the creditor sharing principle from one in which the benefit conferred reduces the asset pool available to creditors collectively.[26] "Creditor transaction" was chosen over "preferential payment" largely as a matter of statutory drafting. A "transaction" occurs when a debtor confers value on another person. A "creditor transaction" is carved out as a transaction in which a debtor confers value on a creditor in satisfaction of a claim. Provisions of the Act that apply to all cases can therefore be drafted as speaking to a "transaction". The fact that a creditor transaction is objectionable to the extent that it has preferential effect is signaled in the title to Part III of the Act.

[26] The rest of this report generally follows the terminology employed in the URTA but uses the current terminology to refer to current law and in some cases

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[24] URTA, s 1 "transaction".

[25] It is worth noting that the title to the US counterpart of the URTA was recently amended by substitution of the word "Transaction" for "Transfer". See Kenneth C Kettering, "The Uniform Voidable Transactions Act; or, the 2014 Amendments to the Uniform Fraudulent Transfer Act" (December 21, 2014) at 29 - 30, Business Lawyer, forthcoming. Available at SSRN: http://ssrn.com/abstract=2541949.

[26] URTA, s 1 "creditor transaction".

juxtaposes the two in order to flag the correspondence between current law and the proposed reforms.

C. Balancing Competing Interests: The Central Policies

[27] Creditors have no need to question a debtor's transactions as long as the value of their debtor's property is sufficient to satisfy all creditors' claims. Conversely, if the debtor does not have enough exigible property to satisfy creditors acting through the judgment enforcement system, nothing is gained by the declaration of a further unenforceable judgment against the debtor. [27] Like existing law, the URTA does not provide for judgment against a debtor who has engaged in behaviour that interferes with creditors' rights. Creditors can satisfy their claims only by recovering property or value from the person who has received it from the debtor. That person is referred to in the URTA and generally as a "transferee". Value gained by a transferee through the actions of a debtor represents a loss to creditors, while a statutory remedy restoring that value to creditors represents a loss to the transferee. The URTA is consciously designed to balance the interests of unpaid creditors with the interests of those who deal with a person who has unpaid creditors.

[28] That balance involves the convergence of two policies. The URTA proceeds on the foundational premise that creditors are entitled to be paid. The primary policy advanced by the Act is that voluntary action taken by debtors should not be allowed to impede their creditors' entitlement to satisfaction of their claims through the means offered by the judgment enforcement system. The Act qualifies that creditor-protection policy through recognition of the competing policy that the law should respect the reasonable expectations of those who deal with a person who has creditors. The transferee-protection policy reflects the need to preserve the finality of legitimate commercial transactions.

[29] The Act employs a combination of strategies to balance the interests of creditors and transferees. Most importantly, the grounds for an order in favour of a creditor are defined in a manner that allows potential transferees to recognize and assess the risk of dealing with a person who may have unpaid

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[27] "Exigible" is the term commonly used to describe property that is not sheltered from judgment enforcement measures by exemptions legislation. See the definition in the CEA, s 1(1)(u). It does not appear in the URTA. The term "property" includes all property, though a few provisions are specifically addressed to exempt property. The term "exempt property" is defined for purposes of those provisions. See s 1(1) "exempt property"

creditors. Other features of the Act, including the flexible order for relief and the short limitation of action period, circumscribe the risk that does exist within reasonable bounds. These points will be elaborated in the discussion that follows.

D. Principal Features of the Act

1. SCOPE OF THE ACT: TRANSFERS OF VALUE

[30] The current provincial law of fraudulent conveyances allows the court to avoid transfers of property by a debtor that hinder or defeat creditors' rights. While transfers of property may have been the primary concern of creditors in Elizabethan England, many other voluntary actions taken by a debtor confer a quantifiable benefit on another person and correspondingly deplete the asset base that would otherwise have been available to his or her creditors. This is recognized to a limited extent in the BIA provisions, under which a "transfer at undervalue" subject to attack by a trustee in bankruptcy includes the provision of services for which no consideration is received by the debtor or for which the consideration received is of conspicuously incommensurate value.[28] The financial worth of a debtor who provides services for free is depleted to the extent of the amount by which it would have increased had they been provided at market rates. The URTA takes a similar approach but goes further through a more comprehensive definition that includes the conferral of a benefit of any kind on another person. Implicitly, the benefit must have a quantifiable monetary value; a non-exclusive list of transactions is provided. For example, a debtor who forgives a debt owed to him or her by another person will have diminished his or her asset base to the extent that it would have been augmented were the debt paid. The net result is the same as if the debtor were paid and then gifted the amount received back to the person who paid it, or to someone else. Release of the debt is a transaction under the statutory definition.

[31] Current fraudulent preferences law is even more limited in scope than is the law of fraudulent conveyances. The *Fraudulent Preferences Act*, allows creditors to challenge a transfer of property *other than money* in satisfaction of a debt.[29] This restriction may have been intended to shelter the ordinary course payment of routine debt from attack, but it produces anomalous and indefensible

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[28] BIA, s 2 "transfer at undervalue".

[29] See *Fraudulent Preferences Act*, RSA 2000, c F-24, s 6(b). For commentary on the effect of this provision, see Dunlop & Buckwold at 1150-52.

results. The scope of the cause of action should be defined in terms that reflect the conditions under which the payment is made, not the medium through which it is effected. The URTA permits creditors to challenge a payment made to another through the conferral of a benefit by any means that directly or indirectly diminishes the paying debtor's asset base if the grounds for relief are established.

2. THE ORDER FOR RELIEF

[32] The *Fraudulent Conveyances Act, 1571* provides that a transfer of property subject to sanction is deemed to be "utterly void, frustrate and of none Effect" but only as against a person "disturbed, hindered, delayed or defrauded". The *Fraudulent Preferences Act* adopts the same approach in relation to both fraudulent preferences actions and fraudulent conveyances actions falling within its scope. The impugned transaction is "void as against any creditor or creditors injured, delayed or prejudiced."

[33] This language raises a number of problems of interpretation.[30] It is not clear whether the transaction in question is void from the outset or merely voidable as declared by the court, or what the precise implications of either interpretation might be, especially taking into account the clear intention that the transaction is void as against some people but not necessarily as against the world at large. The language suggests that the transaction is not void in the literal sense that it either does not exist in law or is to be completely reversed through avoidance. The court is left to the uncertain task of how the statutory language should be given effect through the order granted. What is clear is that the transferee is forced to relinquish in whole or in part the property received from the debtor, or perhaps its value, in favour of the transferor's creditors.

[34] The URTA implements a nuanced and carefully detailed approach to the order for relief. The primary elements of the remedial scheme are threefold. First, the statute states the objective to be attained by the court through the order granted in relation to a Part II or a Part III action, respectively. Second, the court is offered a list of types of order that might be granted alone or in combination to achieve the stated objective. Third, the court is directed to have regard to qualifying factors that will affect the specific terms in which the order is framed.

[35] In the case of a transaction under Part II (transaction at undervalue or one intended to defeat creditors generally), section 16 states that the object of the

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[30] See Dunlop and Buckwold at 1061-64.

order is to make available to the applicant creditor the value conferred on the transferee under the transaction to the extent of the applicant's claim, taking into account the types of orders and the qualifying factors indicated in section 18. The idea is to restore to the applicant creditor the value lost through the transaction. In the case of a creditor transaction under Part III (a preferential payment), section 17 states that the court shall make an order that effectively sets aside the transaction, taking into account the qualifying factors. The idea here is to simply reverse the payment and consequently channel the amount received by the paid creditor into the creditor sharing scheme that was circumvented.

[36] The court may achieve the stated objectives through a range of orders listed in section 18(2), including through a transfer of property or payment of a sum of money by the transferee, a sale of property, the authorization of direct creditor action against property in the hands of the transferee, and various others, some of which are directed to particular types of transaction. The orders contemplated respond to questions for which there are no answers under current law, such as whether a transferee must reimburse creditors for income earned on property received from the debtor that would otherwise have been available to creditors as income of the debtor.

[37] The qualifying factors specified in sections 18(4) and (6) are among the elements of the legislation designed to provide reasonable protection to the interests of transferees who are not complicit in any overt wrongdoing. These are factors that the court is directed to consider in defining the terms of its order.

[38] Section 18(4) applies to an order granted under Part II of the Act; that is, in an application challenging a transaction at undervalue or a transaction intended to obstruct creditors generally as distinguished from an application challenging a preferential creditor transaction. The court is directed to adjust the order in favour of the transferee in recognition of the amount of value given by the transferee, if any, and expenditures increasing the value of property received or generating income from the property, where the order divests the transferee of the property or includes an amount compensating for income earned on the property. A transferee will only be required to disgorge value received from the debtor without consideration given in exchange; the transferee loses the benefit to the extent it was gained gratuitously. To use a simple example, if the transferee paid the debtor $40,000 for an asset worth $100,000, the terms of the order would enable the applicant creditor to recover property or money equivalent to $60,000. The transferee does not lose both the value of the asset and the amount invested in acquiring it. Section 18(4) also directs the court to take

into account actions taken by the transferee in reasonable reliance on the finality of the transaction under which a benefit was received. This provision is designed to allow the court to refuse or limit the extent of an order where a transferee has acted reasonably on a gratuitously received benefit in circumstances such that it would be unfair to order him or her to disgorge its value. While the provision leaves scope for interpretation, it should be applied in a manner that does not undermine the more specific provisions of the Act defining the grounds for relief. The court should not refuse relief merely to protect a sympathetic transferee. The commentary to the Act illustrates the kind of case in which a transferee may not be required to pay for gratuitous value received; for example, when an insolvent debtor pays a reasonable living allowance or provides unremunerated domestic services such as child care to a family member. Although the case would fall strictly within section 7(1)(a), discussed below, the recipient should not be forced to repay the amount of the allowance or reimburse creditors for the value of the services.

[39] Section 18(6) applies to an order for relief under Part III in relation to a preferential creditor payment. The court may adjust the terms of an order to take into account expenditures or investments made by a paid creditor that have increased the value of property received under a creditor transaction if the transferee is divested of the property under the order for relief.

[40] The remedial provisions of the Act also resolve any uncertainty about how property or money recovered from a transferee is to be divided among creditors, where there is more than one. Section 18(3) is designed to refer distribution to the rules that would have applied were the property or money recovered in judgment enforcement action against the debtor. The reference in Alberta would be to the distribution scheme applied by the CEA to the proceeds of writ proceedings taken against property of a judgment debtor. This point is addressed further in Chapter 4.

3. THE GROUNDS FOR RELIEF: TRANSACTIONS AT UNDERVALUE AND TRANSACTIONS INTENDED TO DEFEAT CREDITORS (FRAUDULENT CONVEYANCES)

a. The requirement of intention to hinder or defeat creditors

[41] Section 2 of the *Fraudulent Preferences Act* applies to fraudulent conveyances and requires as a preliminary condition of relief that that the debtor was insolvent or imminently insolvent when he or she undertook the transaction

subject to attack. A creditor who seeks to challenge a transfer of property by a solvent debtor, or one who cannot be proven insolvent at the relevant time, can sue under the *Fraudulent Conveyances Act,1571*, which contains no similar requirement. A more formidable obstacle to success and the most problematic feature of the current law of fraudulent conveyances is that creditors who seek relief under either statute must prove that the debtor intended to hinder or defeat creditors by transferring away the property in question. The requirement is problematic for at least three reasons.

[42] The first problem with the intention test is that it lacks a defensible policy foundation. The law generally assumes that debtors are required to pay their debts regardless of whether they subjectively wish to do so. A debtor who simply doesn't pay a creditor is obliged through the mechanism of judgment enforcement law to give up his or her property to satisfy the debt, regardless of whether non-payment was maliciously motivated. State of mind is not relevant. Similarly, the question of whether a debtor has transferred away property or other value with the intention of defeating creditors is immaterial. What matters is the effect of the transaction on creditors' ability to recover satisfaction. An effects-based test should be the foundation of grounds for relief; a transaction that has the effect of defeating or materially obstructing creditors should be subject to challenge provided that the law takes into account the legitimate interests of the person who has benefitted under it.

[43] The second problem with current law is that the need to prove intention makes litigation highly unpredictable. The courts have adopted and debated a list of evidentiary propositions, some of which are described as "presumptions" and some as "badges of fraud", any of which may or may not be applied in a given case. Most notable is the persistent debate over whether intention to defeat creditors may be inferred from the fact that a transaction has the necessary effect of defeating creditors. Some courts say that intention to defeat creditors irrefutably flows from the proposition that a person must intend the natural consequences of his or her actions, while others suggest that a transaction may be valid if undertaken for a motive other than to do creditors harm.[31] This uncertainty over the principles to be applied is exacerbated by the uncertainty produced by their actual application to a given set of facts. What one judge views as compelling circumstantial evidence of intention to defeat creditors may be regarded by another as legitimate financial planning. A lawyer asked by a client

[31] See Dunlop & Buckwold at 1026-39.

whether a particular transaction is or is not afoul of the law will generally be forced to offer a highly conditional answer.

[44] The problem of uncertain outcomes is particularly great where the debtor has transferred property in a transaction prejudicial to creditors in exchange for some amount of consideration. A creditor who can prove that the debtor intended to hinder or delay creditors can have the transaction avoided only if the transferee knew of the debtor's intent in the sense deemed material. The courts have struggled both to determine what amount of consideration makes a transfer one for value within the scope of this principle, and to define the degree of knowledge on the part of a transferee that justifies avoidance. Notice or knowledge that the transaction would harm the transferor's creditors is not necessarily sufficient; the transferee must likely be in some way complicit in the debtor's intention to obstruct them.[32] To complicate matters further, it is not clear where the burden of proof lies in relation to the transferee's state of mind. Must the plaintiff prove that the transferee has the proscribed degree of knowledge of the debtor's intention, or must the transferee prove lack of knowledge by way of defence?

[45] Finally, the factual and evidentiary burden of proving state of mind means that creditors will often not undertake the daunting and expensive project of seeking to recover property lost to them through their debtor's activities.

[46] To summarize, the intention test as the foundation of current law represents unsound policy, produces unpredictable outcomes and operates as a disincentive to creditor action; the law is highly ineffective as a device for protecting creditors' rights under the judgment enforcement regime. The solution adopted by the URTA is to offer three grounds for relief, all of which depend on the effect of the transaction on creditors' rights of recovery and the most significant of which has no regard to the intention prompting the transaction in question. The three grounds for relief are defined respectively by sections 7(1)(a), 7(1)(b) and 7(1)(c).

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[32] The state of the law is described as follows by Dunlop & Buckwold at 1054:

> Puzzling" is a fair description of the courts' continuing struggle to decide what evidence regarding the transferee is need to prevent the conveyance for consideration from being safe from a creditor's fraudulent conveyance action.... The courts have developed a smorgasbord of inconsistent and conflicting tests for deciding whether the transferee's state of mind deprives them of the defence. Commentators and law reform commissions have underlined the lack of one dominant test and the resulting confusion and muddle.

b. Grounds for relief under the URTA

i. The debtor is insolvent and receives no consideration or consideration worth conspicuously less than the value given: section 7(1)(a)

[47] Creditors seeking redress under the URTA undoubtedly rely most often on section 7(1)(a) as grounds for relief. That section offers a remedy if the debtor is presently or imminently insolvent at the date of a transaction and the transferee receives property or other economic benefit from the debtor for no consideration or for consideration worth conspicuously less than the value received; that is, the transaction is wholly or substantially a gift. Since an insolvent debtor is by definition unable to satisfy creditors' claims, a transfer of value that diminishes the debtor's asset base correspondingly diminishes the ability of creditors to recover and necessarily hinders or defeats their rights. While the debtor's intention is not a factor in the cause of action, one may assume that an insolvent or nearly insolvent debtor is or should be aware that a course of action depleting his or her asset base will have an adverse effect on creditors.

[48] On the surface, URTA section 7(1)(a) proceeds entirely on the basis of the creditor-protection policy. However, it implicitly embodies the balancing of interests discussed under heading C above. A transferee stands to lose the benefit received from the debtor only if he or she gave no consideration at all in exchange, or the consideration given was "conspicuously less" than the value given by the debtor. This approach gives effect to the policy that a person who deals with a debtor should be vulnerable only if they are in a position to recognize the risk inherent in the transaction presented. The term "conspicuously less" denotes that it would be obvious to a reasonable person dealing with the debtor under the circumstances in question that they are getting a deal that might be described in non-legal terms as "too good to be true". A person who is offered property or another benefit for conspicuously less than the consideration paid should be alert to the likelihood that the debtor is in serious financial straits or otherwise prompted by motives that may be legally suspect. A transferee who does deal with a debtor on terms falling within section 7(1)(a) is sheltered by the remedial scheme of the Act, discussed further below. One who is not privy to a deliberate scheme to defeat creditors stands to lose the value received in excess of the consideration given but will be allowed to retain or recover the amount actually paid.

[49] The approach represented by section 7(1)(a) is not novel. It was introduced in the United States in 1918 under a statute proposed by the National Conference of Commissioners on Uniform State Laws, called the *Uniform*

Fraudulent Conveyances Act, and has been a feature of the law of most states for many decades. Creditors could challenge a transfer of property under that Act if a debtor did not receive "fair consideration" from the transferee and the debtor was insolvent or would be rendered insolvent by the transaction.[33] The test as revised in the re-named *Uniform Fraudulent Transfers Act* in 1984 required creditors to prove only that the debtor did not receive "reasonably equivalent value".[34] The change in wording was designed to establish that the transferee's good faith is not a factor in determining the adequacy of the consideration given.[35] American law was and is grounded on our shared English legal heritage as represented by the *Fraudulent Conveyances Act, 1571* and, like the URTA, it provides alternative grounds for relief where a transaction is intended to defeat creditors, regardless of the consideration exchanged.[36] The lack of an intention requirement when the challenged transaction involves an insolvent debtor who receives less than the value given to the transferee has clearly proven to be a satisfactory approach, even though the test of less than "reasonably equivalent value" given for the benefit received from the debtor is significantly less protective of transferees than the URTA test of consideration "conspicuously less than" the benefit received. There was no movement to revise this part of the Act when it was amended in 2014 to add a choice of law provision and make other relatively minor adjustments, including a further change in title to the *Uniform Voidable Transactions Act*.

[50] The ULCC working group did not attempt to define what is "conspicuously less" than value received from the debtor. Its meaning is self-evident and further elaboration is as likely to obfuscate as to clarify. The question is one of judgment. Is it obvious that the transferee paid far too little for what he or she got from the debtor? Would a reasonable person dealing with the debtor under the circumstances prevailing at the time have regarded the amount paid as

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[33] The statute does not refer to the debtor's state as "insolvent" but describes circumstances that amount to insolvency as it is generally understood, being either insufficient assets to satisfy debts or inability to pay debts as they become due. See the *Uniform Fraudulent Transfers Act*, National Conference of Commissioners on Uniform State Laws, 1984, §4(a)(2) (renamed the *Uniform Voidable Transactions Act*, National Conference of Commissioners on Uniform State Laws, 2014).

[34] As at 2014, the *Uniform Fraudulent Transfers Act* was in force in 43 states while the *Uniform Fraudulent Conveyances Act* remained in force in two.

[35] See the *Uniform Fraudulent Transfers Act*, National Conference of Commissioners on Uniform State Laws, 1984, (renamed the *Uniform Voidable Transactions Act*, National Conference of Commissioners on Uniform State Laws, 2014), Official Comment, §3.

[36] For a short history of American law and the correspondence between state law and federal bankruptcy law, see Kenneth C Kettering, "The Uniform Voidable Transactions Act; or, the 2014 Amendments to the Uniform Fraudulent Transfer Act" (December 21, 2014) at 29 – 30, Business Lawyer, forthcoming. Available at SSRN: http://ssrn.com/abstract=2541949.

obviously and substantially less than the value received? Any kind of mathematical test would be potentially over-inclusive or under-inclusive in any given case and its application would depend on the court's ability to precisely and accurately value the benefits exchanged. For example, if conspicuously less than commensurate value were defined as 40% or less, the court would be required to determine if the value given by a transfer was 39% or 41% of what was received, and the test would discriminate between transactions on the basis of a 1 or 2 percentage difference in value. Furthermore, a difference of 20% in values exchanged might be a conspicuous discrepancy in a multi-million dollar transaction but nothing more than a good sale price in a $500 transaction. Even an 80% discount might not constitute a conspicuously low price in the context of a retail sale of relatively low value consumer goods; it depends on the circumstances. The BIA adopts a similar test in the provisions addressing a transfer at undervalue, which are defined as "a disposition of property or provision of services for which no consideration is received by the debtor or for which the consideration received by the debtor is conspicuously less than the fair market value of the consideration given by the debtor."[37] The working group chose not to include a reference to "fair market value" in its formulation on the view that it could confuse the issue of whether valuation is to be based on ordinary market rates or on the circumstances of the actual transaction, which might be such that market rates are inappropriate.

ii. The debtor intends to and does obstruct creditors: sections 7(1)(b) and 7(1)(c)

[51] The URTA overcomes the primary source of difficulty under current law by abandoning proof that the debtor intended to hinder creditors as the basis for relief under the grounds defined by section 7(1)(a). However, it recognizes that relief should be available where a debtor does intend to defeat or obstruct creditors by means of a transaction and succeeds in that objective, if the circumstances are such that the transferee is in a position to recognize the risk of losing the benefit received. This is accomplished by the provision of two intention-based grounds for relief, represented by sections 7(1)(b) and 7(1)(c), respectively.

[52] Section 7(1)(b) offers relief when the debtor's primary intention is to hinder or defeat recovery by creditors if in fact the transaction has that effect and the debtor receives no consideration from the transferee or consideration worth

[37] The BIA provisions differ from those of the URTA in other respects, most notably in retention of an intention requirement as grounds for attacking a transaction.

conspicuously less than the value of the benefit conferred by the debtor. As under section 7(1)(a), the transferee who receives a gratuitous benefit or gives "conspicuously less" than what he or she received from the debtor is in a position to recognize that the transaction may be suspect and to decide accordingly whether or not to proceed.

[53] Section 7(1)(c) offers relief where debtor and transferee were complicit in a plan to defeat or obstruct the debtor's creditors. The risk of the transaction is clearly apparent to the transferee in such a case. A transferee who knows that the transaction was intended by the debtor to obstruct creditors cannot claim the benefit of the factors that would otherwise qualify an order for relief under section 18(4). In other words, the transferee will not be permitted to retain or recover any value invested in the transaction or in property received under it.[38]

[54] Sections 7(1)(b) and (c) both require proof that the challenged transaction materially hindered creditors' ability to recover. As pointed out in the commentary to section 7, this requirement will rarely be met where the debtor is solvent, since solvency generally means that the debtor has property or an income stream against which a judgment may be enforced. However, a solvent debtor may successfully hinder creditors by removing property from the jurisdiction or converting it into a form that is otherwise difficult to reach under judgment enforcement measures.

[55] Proof of intention is addressed in section 7(3), which offers a non-exclusive list of factors that the court may consider in determining the intention of the parties to a transaction.

iii. Special Cases

[56] Current law offers one set of rules for attacking all transfers of property that have the effect of hindering or defeating creditors. This produces uncertain and unfair results in some cases, the most significant of which are those involving payments of money and transfers of property in satisfaction of legally recognized spousal claims to support and division of property. Questions abound. Is a transfer of property pursuant to a spousal property settlement void or valid according to whether a debtor-transferor was or was not conscious of its effect on his or her creditors' rights of recovery? Can a transfer of property under a bona fide separation agreement or court order be undone if it is subsequently

[38] URTA, s 18(5).

challenged by creditors of the transferring spouse? How can a lawyer properly advise a client with respect to such an agreement or order without delving into the mind of the other spouse or former spouse?

[57] The URTA includes provisions dealing specifically with transactions between spouses whose relationship is no longer intact where the transaction is effected by a separation agreement, as defined, or a court order for division of property or support. Such transactions, designated "spousal transactions", may only be challenged under the grounds prescribed by section 7(1)(c); that is, only where the parties collusively intended to defeat the creditors of one of them. The rationale for this approach is discussed in the commentary to section 8(1). The essential question is whether the transaction is jointly intended by the parties as a creditor avoidance device or as a legitimate settlement of spousal and family affairs necessitated by the breakdown of their relationship. A failure to fully disclose creditors' claims in an action for support or division of property or an attempt by either or both parties to hide facts material to relief under the Act are among the factors that the court is invited to consider as evidence of intention to avoid creditors.

[58] Section 8 of the URTA also restricts the grounds for relief in relation to three other categories of transaction; a transaction under which a debtor refuses to act under a power of appointment, a transaction involving the provision of a guarantee or indemnity, and a transaction other than a spousal transaction that is effected by an order of the court. The first two cases are treated in the same way as spousal transactions; creditors are entitled to relief only under section 7(1)(c).[39] In the case of non-spousal transactions effected by court order, creditors are entitled to relief on the grounds established in either section 7(1)(b) or (c).[40] Both require proof that the transferor intended to hinder or defeat creditors by means of the transaction and achieved that result. The commentary to section 8 sets out the rationale for and operation of the provisions governing these exceptional cases.

[59] Section 9 deals with the special case of transactions that consist of the purchase or redemption of its own shares by a debtor corporation or the payment of dividends. These rules are designed to supplement and interface with provisions of the *Canada Business Corporations Act* and Alberta *Business Corporations Act* [ABCA] that apply to the authorization of such payments by

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[39] URTA ss 8(2)(b) and (c).

[40] URTA s 8(3).

insolvent corporations.[41] The URTA provisions differ from those of the corporations statutes in that the latter provide for recovery by the corporation from directors who have authorized the payment and from shareholders who have received it.[42] The URTA allows creditors to recover from the shareholder who was paid and potentially from a director who authorized the payment. Directors and shareholders are shielded from "double jeopardy" through the stipulation that a person against whom an order is granted under a corporations statute is not subject to an order under the URTA. If the URTA is enacted, consideration should be given to amending the ABCA to reciprocally provide that a person against whom an order is granted under the URTA is not subject to an order under the ABCA.

4. THE GROUNDS FOR RELIEF: CREDITOR TRANSACTIONS (FRAUDULENT PREFERENCES)

a. The requirement of intention to hinder or defeat creditors

[60] Like the law of fraudulent conveyances, the current law of fraudulent preferences provides a remedy where a debtor intends to harm creditors; in this case, where the debtor transfers property to a creditor "with intent to give that creditor a preference" over another creditor or creditors. The problems associated with the intention requirement as it applies here are essentially the same as those that accompany the intention requirement of fraudulent conveyances law. It advances the wrong policy, creates uncertain outcomes and presents evidentiary obstacles that make it very difficult for creditors to successfully challenge a payment that violates their right to share.

[61] Anti-preference law interferes with the payment of debt by requiring the paid creditor to disgorge a payment received so it may be allocated proportionally among the creditors of the paying debtor. This is justified by the need to protect the creditor sharing regime established by law. The creditor sharing principle is recognized and implemented to the fullest extent under the law of bankruptcy. The property of a bankrupt debtor is liquidated by the trustee and divided among creditors in accordance with the distribution scheme

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[41] *Canada Business Corporations Act*, RSC 1985, c C-44; Alberta *Business Corporations Act*, RSA 2000, c B-9 [ABCA].

[42] Creditors may apply for an order under the ABCA requiring a shareholder to restore to the corporation money paid in contravention of the applicable provisions of the Act but the court is not authorized to make an order in favour of the creditors, and creditors have no rights against a director who authorized a payment. See ABCA, s 118.

imposed by the BIA. Subject to the prior right of payment granted to secured and preferred creditors, unsecured creditors are to be paid through allocation of the bankrupt's estate *pro rata* in proportion to the amount of their claims. The BIA includes provisions designed to prevent debtors and creditors from circumventing the distribution scheme through pre-bankruptcy payments made to select creditors. A paid creditor is preferred over others to the extent that he or she recovers more than would have been recovered under a bankruptcy distribution. Outside of bankruptcy, the right of debtors to pay creditors as they wish is qualified by the creditors' relief legislation described in Chapter 2 of this report under heading C. Provincial anti-preference law is justified by the need to protect the creditor sharing rules embodied in judgment enforcement law through the provisions of Part 11 of the CEA.

[62] The payment of one creditor harms others in a legally materially sense only if it interferes with their existing or potential right to share under a law that implements the creditor sharing principle. As a matter of policy, there is no good reason to differentiate between payments that may be challenged and those that may not on the basis of whether the debtor intended to give a preference. The harm does not flow from the debtor's intention in making the payment, for good or ill. It flows from the effect of the payment. In spite of its apparent deference to intention as the foundation of relief, the *Fraudulent Preferences Act* recognizes this through an effects-based rule that supplements the intention requirement. Subject to restrictions discussed elsewhere, a payment made by an insolvent or nearly insolvent debtor is void as against creditors if it has the effect of giving the paid creditor a preference and is challenged within one year of its date.[43] Unfortunately, it is not at all clear when a payment has the effect of giving a preference. While section 4 purports to define a transaction that is deemed to do so, the meaning of the provision is obscure.[44] The debtor-intention requirement prevails when the effects-based rule cannot be applied.

[63] Aside from its dubious foundation in policy, the debtor intention requirement makes for great uncertainty in any advising lawyer's attempt to predict the outcome of potential litigation.[45] Judges have decided that a payment cannot be set aside if the debtor's *dominant* motive was something other than the conferral of a preference, even though the debtor may have recognized that the

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[43] *Fraudulent Preferences Act*, RSA 2000, c F-24, s 3.

[44] See Dunlop & Buckwold at 1121 – 37 for a full discussion of the problems associated with application of the effects-based rule.

[45] The problems outlined here are discussed in detail in Dunlop & Buckwold at 1096 - 1120.

payment would have preferential effect. A payment stands if it was made in response to pressure exerted by the paid creditor or in the hope of remaining in business, or if prompted by various other motives regarded as legitimate. Furthermore, the courts require a creditor who challenges a fraudulent preference to establish at least that the paid creditor knew that the paying debtor intended to confer a preference and, in many cases, that the paid creditor actively participated in that objective, even though the statute makes no reference to the paid creditor`s state of mind.

[64] The need to prove intention to prefer by the debtor along with culpable knowledge or intention on the part of the paid creditor imposes an extremely challenging evidentiary burden on creditors who might seek to invoke the *Fraudulent Preferences Act*. Other obstacles include the limited scope of the Act which allows creditors to challenge only payments made through the transfer of property other than money.[46]

b. Grounds for relief under the URTA

[65] The URTA implements the foundational policy that payments to creditors may be challenged if they undermine the right of creditors to recover satisfaction through resort to the property of their joint debtor according to a sharing scheme imposed by law. What matters is not whether the debtor intended to prefer one creditor over others, but whether the effect of a payment is that the recipient is paid proportionately more. However, that policy operates with less force under provincial law than it does in bankruptcy, where it is most fully implemented. Provincial law does not impose a general rule under which creditors are entitled to be paid proportionately. It requires a creditor to share only if he or she takes steps to recover payment through enforcement of a judgment, and even then the distribution rules of the CEA require sharing of the proceeds of enforcement action only among judgment creditors who have registered a writ of enforcement against the debtor, not among unpaid creditors generally. The limited operation of the creditor sharing principle under provincial law suggests that provincial preferences law should be limited in scope and, to the extent possible, should be consistent with the anti-preference rules of the BIA.[47]

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[46] *Fraudulent Preferences Act*, RSA 2000, c F-24, s 9(a).

[47] See Reform of Fraudulent Conveyances and Fraudulent Preferences Law, Part 2: Preferential Transfers, Final Report of the Working Group (Winnipeg 2011), online: Uniform Law Conference of Canada <www.ulcc.ca/images/stories/2011_pdf_en/2011ulcc0005.pdf>, at 3 - 5.

[66] The restricted application of the sharing principle as implemented in the CEA presents a technical challenge in determining when a payment has preferential effect. In principle, a definitional rule would require valuation of the debtor's assets available for the satisfaction of creditors' claims relative to the individual and cumulative amounts owed to creditors who qualify to share in those assets, which in turn would require identification of the class of creditors whose claims count under the sharing principle and the date at which their claims must be assessed.[48] The problems described above in relation to the effects-based provision of the *Fraudulent Preferences Act* confirm the difficulties involved. The solution adopted by the URTA is relatively simple, produces predictable outcomes, is consistent with the BIA and is defensible as a matter of policy.

[67] Under section 18(1), a creditor transaction may be set aside if the creditor receiving payment was not dealing at arm's length with the debtor in relation to the payment and the debtor was insolvent or verging on insolvency when the payment was made. The remaining subsections of section 18 are designed to incorporate by reference the provisions of the BIA that determine when people are at arm's length. This aligns the anti-preference rules of the URTA with the BIA rules that apply to a payment by an insolvent person to a non-arm's length creditor during the 12 months preceding bankruptcy.

[68] This extract from the working group report explains the rationale for section 18:[49]

> [11] A payment by a debtor who is insolvent or becomes insolvent shortly thereafter will almost invariably constitute a preference in fact. Since the state of insolvency means that the debtor is by definition unable to satisfy all creditors in full, the creditor who is paid voluntarily will receive a proportionately greater recovery than those creditors who are not.... [T]he payment of one of two or more creditors by an insolvent debtor in itself produces a preference in the vast majority of cases. In the result, the circumstances that constitute a voidable preference under the BIA are substantially the same as those that constitute a preferential payment under the proposed legislation, though the rules are formulated differently.

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[48] For example, should the calculation take into account only amounts owed to existing writ-holders, or should it include the claims of all creditors who might obtain judgment and issue a writ?

[49] Reform of Fraudulent Conveyances and Fraudulent Preferences Law, Part 2: Preferential Transfers, Final Report of the Working Group (Winnipeg 2011), online: Uniform Law Conference of Canada <www.ulcc.ca/images/stories/2011_pdf_en/2011ulcc0005.pdf>.

[69] This approach both adopts a clear effects-based rule and balances the interests of a transferee-creditor who receives payment with those of creditors generally. A creditor who is not dealing at arm's length with the debtor in relation to the payment in question is in a position to know or at least strongly suspect that the debtor is insolvent or in precarious financial circumstances and that anti-preference law may be invoked by the payment. As in the case of transactions at undervalue, the grounds for relief are defined in terms that facilitate a reasonable assessment of risk on the part of a person who receives property from a debtor.

[70] The working group recognized that a creditor who is at arm's length from the debtor will sometimes know that the debtor is insolvent and that a payment received may have the practical effect of preferring that creditor over others who will remain unpaid. However, it concluded that it is not necessary or advisable to include arm's length payments within the scope of the Act. As noted earlier, preferential payment is primarily a matter of concern under bankruptcy and insolvency law, which, subject to the legislated priority granted to identified creditors offers *pro rata* recovery from the residual estate of the debtor to all unsecured creditors regardless of whether their claim has been reduced to judgment. Creditors do not have a comparable right to share in their debtor's assets under provincial law, which extends the sharing principle to a very limited class of creditors claiming against the proceeds of a specific asset or asset pool recovered through formal judgement enforcement measures taken by one of them. Grounds for relief that would allow creditors to recover arm's length payment on the basis of the debtor's insolvency alone would expand the operation of provincial preferences law far beyond the bounds of both federal preferences law and the limited sharing regime contemplated by judgment enforcement law, and the definition of grounds for relief that include a knowledge requirement would invite the sort of uncertainty in outcome that reform is designed to overcome. The decision to restrict the application of the Act to non-arm's length payments is explained by the working group as follows:[50]

> [14] The recommendations of the working group allow only payments to non-arm's length creditors of an insolvent or nearly insolvent debtor to be recovered by other creditors. Payments to arm's length creditors are not vulnerable. This approach is supported by the general policies of limited interference with the payment of creditors

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[50] Reform of Fraudulent Conveyances and Fraudulent Preferences Law, Part 2: Preferential Transfers, Final Report of the Working Group (Winnipeg 2011), online: Uniform Law Conference of Canada <www.ulcc.ca/images/stories/2011_pdf_en/2011ulcc0005.pdf>.

> and substantial consistency with the BIA, outlined above. Payments to arm's length creditors can rarely be challenged under the BIA; they are void only if made [by an insolvent debtor][51] within the 3 month period prior to bankruptcy and the debtor intended to give the recipient creditor a preference over another creditor. Although a presumption of intention to prefer arises from the preferential effect of a payment, the presumption is readily rebutted (e.g. the payment is made in the "ordinary course", the debtor's dominant intention was to remain in business or the payment was elicited by a "diligent creditor" through ordinary collection measures). The creation of a provincial cause of action designed to maintain the desired consistency of approach with the BIA would require the imposition of a 3 month limitation period and retention of the intention to prefer test that is a primary factor in the dysfunctional state of existing law. Such an approach would serve only to create uncertainty without offering creditors any meaningful protection against disproportionate voluntary payments.
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> [15] The decision to exempt arm's length payments from challenge is inferentially supported by the approach taken in other countries and by existing law, all of which implement a policy of limited intervention. The preference rules that apply under the bankruptcy law of other jurisdictions protect arm's length payments by various means, whether by requiring proof of intention to prefer, exempting "ordinary course" payments or sheltering recipients who were unaware of the debtor's fragile financial circumstances. All are plagued by uncertainty and none have proven entirely satisfactory. Although payments to arm's length creditors can in theory be challenged as preferences under current provincial law, the substantial restrictions imposed and defences offered by the legislation mean that the theory rarely bears out in practice. Successful preference actions almost always involve payments to non-arm's length creditors and in practice arm's length creditors are rarely party to a calculated attempt to avoid the creditors' relief law that would otherwise limit their recovery to a proportionate share of the debtor's non-exempt assets. In short, the law generally does not permit interference with arm's length payments. Little is to be gained by attempting to devise rules that will separate legitimate from wrongful arm's length payments and whatever modest benefits might be achieved would be outweighed by the costs flowing from the uncertain outcomes produced by ambiguous rules.

This approach also avoids the very substantial problem of drafting an intelligible rule that would provide for relief against arm's length payments deemed

[51] The bracketed words are added to the text of the report for clarification.

objectionable on defensible policy grounds while protecting routine payments from challenge.

[71] The URTA abandons the distinction made in the *Fraudulent Preferences Act* between payments of money, which are not subject to challenge, and payments effected by a transfer of property of another kind. As the foregoing extract suggests, the need to leave payments that might be regarded as routine or "ordinary course" untouched is met by restricting the anti-preference rules to non-arm's length payments. Payments of money by an insolvent debtor to a person who is not at arm's length in relation to the payment are not ordinary course in the sense that the recipient would not anticipate a claim for relief by other creditors. The URTA therefore expands the scope of provincial preferences law by allowing creditors to recover payments of money, but restricts its operation to payments among parties whose proximity of relationship is likely to entail a shared financial interest.

5. STANDING TO SEEK RELIEF

[72] The question of who may challenge a fraudulent conveyance under current law is remarkably perplexing. Section 2 of the *Fraudulent Preferences Act*, which addresses fraudulent conveyances rather than fraudulent preferences, provides that a transfer of property by an insolvent or nearly insolvent person with intent to defeat "the person's creditors or any one or more of them is void as against any creditor or creditors injured…." This is taken to mean that only a person who is a creditor at the date of the transaction in question has standing to seek redress under the Act. In contrast, the *Fraudulent Conveyances Act, 1571* is addressed to transfers intended to harm "creditors and others". As interpreted by the courts, the word "others" allows a person whose claim arose after the date of the impugned transaction to sue. Substantial case law exists on the question of who is a "creditor" under either statute, and likely more on the difficult question of who qualifies as an "other" under the *Fraudulent Conveyances Act, 1571*. It suffices here to say that the rules of standing are complex, uncertain and greatly in need of clarification.[52]

[73] Standing to challenge a fraudulent preference under the *Fraudulent Preferences Act* is comparatively clear, in that only a person who is a creditor at

[52] For a full discussion of the question of standing, see Dunlop & Buckwold, at 991 - 1005.

the time of the preferential payment may challenge it. The case law determining who is a "creditor" is relevant here as well.

[74] The URTA resolves the uncertainties of current law on the related questions of who has standing to challenge a transaction and when a person who has standing may commence proceedings under the Act. Standing under Parts II and III respectively will be discussed separately.

[75] The first condition of standing under Part II is that a person seeking relief must hold a "claim" against the debtor as defined in section 1, which is a claim in law that may result in a money judgment. Section 6 speaks to the date at which the claim must have arisen. A person who has a claim at the date of the transaction in question may challenge it under any of the grounds for relief; that is, on the grounds that the debtor was insolvent or imminently insolvent and the transaction depleted his or her asset base because no consideration or conspicuously little consideration was received from the transferee in exchange for the value given, or on the intention-based grounds. Section 6(2) ensures that a person who has commenced an action on a claim that has not yet been proven by judgment before the transaction occurred has standing under that rule.

[76] A transaction that falls within the grounds for relief inherently prejudices creditors who hold claims at the time it occurs. Those whose claims arise after the transaction are in a different position. While they may not recover what they are owed in full or at all, that result flows from the debtor's financial circumstances at the time the claim arose, not from a transaction that predated it. They are in the same position they would have been in if the debtor had never had the property lost. A person whose claim arose after the date of a transaction may therefore challenge it only under the intention-based grounds for relief; that is, only when the transaction was intended by the debtor to impede existing or anticipated creditors and it in fact had that consequence. This ensures that a debtor cannot intentionally avoid an anticipated future claim by transferring away assets before the claim materializes.

[77] The rules of standing in an application under Part III are defined in section 12 and are relatively simple. Only a person who has a claim at the date of a creditor transaction may seek an order for relief. This follows from the fact that a payment can only have preferential effect relative to the claims of existing creditors. Future creditors have no right to share.

[78] Sections 6 and 12 confer standing on the substantive basis that a person has a claim against a debtor the enforcement of which is prejudiced by a

transaction between the debtor and a transferee. Section 5 determines when a person who has such a claim may commence an action under the URTA for relief against the transferee who has benefited by the debtor's action. A person who has a claim against the debtor need not have reduced that claim to judgment in order to commence an action challenging the transaction. However, a person who applies for relief cannot benefit under an order against the transferee-defendant until the applicant's claim against the debtor has been proven by judgment, either in a separate proceeding or through joinder of the debtor in the URTA action. The transferee is liable only to a person who has a claim that is demonstrably valid and enforceable through judgment enforcement proceedings against property of the debtor. A person who does not have judgment against the debtor must commence an application under the URTA in time to avoid foreclosure of relief against the transferee by the relatively short limitation of actions period imposed and then seek a stay of proceedings if necessary to accommodate whatever steps may be required to obtain judgment on the claim against the debtor.

6. TRANSACTIONS INVOLVING EXEMPT PROPERTY

a. The function of exempt property

[79] The term "exempt" here refers to property that is legislatively exempted from judgment enforcement measures against its owner. Conversely, "exigible" property is property that is not exempt so is subject to judgment enforcement measures. Exemptions law is generally designed to ensure that a judgment debtor is permitted to retain sufficient property and income to live and to support his or her family at a basic level of existence, presently and in the future. Alberta exemptions law shelters a judgment debtor's property and employment earnings to a relatively modest extent, with the notable exceptions of the farm residence and equipment exemptions, the exemption of insured annuities and the recently enacted exemptions protecting registered investment plans. Regardless of its extent, exemptions law is justified by the function the exempt property serves in the life of the debtor and his or her family.

[80] The design of a law governing a debtor's dealings with exempt property raises two questions of policy. First, should relief be available against a transferee who receives property that was exempt in the hands of a transferor-debtor? Second, should the law allow creditors to claim exempt property procured by a debtor in exchange for exigible property?

b. Transfers of exempt property

[81] Neither the statutes governing fraudulent conveyances and fraudulent preferences nor exemptions legislation speaks to the question of whether creditors are entitled to claim exempt property transferred by a debtor to another person. Alberta courts have generally concluded that they are not. This view presumes that the transfer does not represent a loss to creditors. If they could not enforce against the property in the hands of the debtor, they lose nothing when the debtor disposes of it. The ULCC working group was initially persuaded by that view and recommended that it be incorporated in reformed legislation. However, reaction to that recommendation prompted reconsideration resulting in the revised recommendation implemented by the URTA. Creditors may recover property transferred away by the debtor if the transfer falls within the grounds for relief, regardless of whether the property was exempt in the hands of the debtor.

[82] This approach draws support from the rationale for exemptions law. Property is exempt only while it serves the function protected by exemptions legislation. For example, a person who ceases to be a farmer can no longer claim an exemption for agricultural equipment that he or she is no longer using to earn farm income. Similarly, a debtor who transfers an exempt asset to someone else has implicitly decided that the item in question is no longer required for the purpose protected by the exemption; the exemption is abandoned with respect to that item for that debtor. If a different asset of the same kind is acquired in substitution, the exemption will attach to the new asset. There is no reason to protect the property in question from creditors once it is no longer being used by the debtor for the purpose the exemption is designed to serve.

[83] The approach adopted in the URTA also avoids the potential doubling of an exemption. Assume that a debtor owns a truck worth $5,000, which is currently the amount of the motor vehicle exemption under the CEA and the *Civil Enforcement Regulation* [CER].[53] If the debtor gives the truck to her son and then purchases a car, the debtor will be entitled to claim a $5,000 exemption with respect to the car. If creditors could not recover the truck, $10,000 worth of property belonging to the debtor would be effectively exempted from judgment enforcement.

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[53] CEA, s 88(d); *Civil Enforcement Regulation*, AR 276/1995, s 37(1)(c) [CER].

[84] The URTA incidentally resolves an ambiguity in the legislation currently governing writs binding land. The CEA provides that a writ registered under the *Land Titles Act* binds the enforcement debtor's "exigible land" described in the certificate of title.[54] The *Land Titles Act* provides that registration of a writ binds "all legal and equitable interests of the debtor" in the land included in the certificate of title.[55] The different wording has different consequences where a debtor conveys to another person land that attracts a principal residence exemption under the CEA. If the wording in the *Land Titles Act* governs, the transferee acquires the land subject to a writ registered against title and the writ can be enforced against the transferee if it is not his or her principal residence.[56] If the wording of the CEA governs, the land is not bound by the writ at all to the extent of the exemption. The transferee therefore acquires the land free of the writ, in the case of a farm homestead, or free of the writ to the extent of the transferor's exemption, in the case of a non-farm principal residence. Under the approach taken in the URTA, creditors may challenge the transaction regardless of whether the land was exempt in the hands of the debtor-transferor and the outcome will be the same whether the writ does or does not follow into the hands of the transferee.

[85] The decision to allow creditors to seek relief against a transferee of exempt property creates a potential problem if the debtor continues to use the property post-transfer for the function attracting the exemption. This is most likely to occur in relation to the debtor's home but could arise in other contexts as well. For example, a farm debtor might convey title to his or her farm residence to a daughter or son but continue to farm and continue to reside in the house. Section 20 responds to the problem by allowing the court to suspend the enforcement of an order for relief against the transferee until the debtor ceases to use the property in the manner attracting the exemption and, if such an order is granted, to order that a writ be registered against the transferee or the property. This provision reflects an approach that has been taken by the courts in some

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[54] CEA, s 33(2)(b).

[55] *Land Titles Act*, RSA 2000, c L-4, s 122(7).

[56] This feature of the law in other jurisdictions was one of the factors taken into account by the ULCC working group. If a writ binds exempt land when registered against the title but the URTA precludes relief against a transferee of that land, the ability of creditors to enforce against the land after it is transferred to another person could depend on the fortuitous timing of procurement of judgment and consequent registration of a writ. If a writ has not been registered before the transfer occurs and a transfer of exempt land cannot be challenged, creditors will have no claim to the land as against the transferee. If a writ has been registered before the transfer occurs, creditors can claim it in the hands of the transferee regardless of whether it was exempt in the hands of the debtor/transferor.

jurisdictions under current law.[57] The result is to protect the property as long as it continues to be used by the debtor for the exempt purpose.

c. Transfers of non-exempt property in exchange for property that is exempt

[86] Under the URTA, a transaction that involves the exchange of non-exempt for exempt property may be challenged only if it falls within the ordinary grounds for relief. In practice, this means that such a transaction is not subject to challenge if the values exchanged are reasonably equivalent, unless the parties to the transaction are complicit in an attempt to hinder or defeat the transferor's creditors.[58] From a financial point of view, the loss to creditors is likely to be greatest when a debtor invests exigible funds in the purchase of a principal residence or in an RRSP or other registered plan that attracts a statutory exemption.[59] While some would argue that a debtor should not be permitted to shelter assets from creditors by exchanging non-exempt for exempt property, the policies supporting the approach recommended by the ULCC working group and incorporated in the URTA are persuasive. Its implications are explained in the working group report:[60]

> [44] The ... recommendation reflects the need to respect the policies embodied in exemptions legislation. Property declared by statute to be exempt in the hands of a debtor is protected on the grounds of the function that property is perceived to have in relation to the ability of the debtor to maintain him or herself and his or her family. There is little distinction between the conduct of a debtor who purchases such property using non-exempt assets in the knowledge that creditors will be denied their recovery and that of a debtor who holds exempt assets previously acquired in the knowledge that he or she could by relinquishing them satisfy creditors' claims. The shades of distinction that exist will often be too subtle to legitimately subject one circumstance to legal penalty while sheltering another.

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[57] See *Petryshyn v Kochan*, [1940] 2 WWR 353 (Sask KB). This provision might be revised for purposes of enactment in Alberta to provide for the registration of an attachment order rather than a writ. See further Chapter 4 heading B(2) of this report.

[58] The case would fall within URTA s 7(1)(c).

[59] For the principal residence exemption, see CEA s 88(g) declaring the exemption and CER s 37(1)(e) establishing the amount of the exemption. A farmer's principal residence is exempt under CER s 88(f) to the extent of 160 acres, regardless of value. For the exemption of registered plans, see CEA s 81.1 and see CER ss 40.1 and 40.2 regarding payments out of a registered plan.

[60] Reform of Fraudulent Conveyances and Fraudulent Preferences Law (Transactions at Undervalue and Preferential Transfers), Part 1: Transactions at Undervalue & Fraudulent Transactions, Final Report of the Working Group (Halifax 2010), online: Uniform Law Conference of Canada <www.ulcc.ca/images/stories/2010_pdf_en/2010ulcc0032_Fraudulent_Conveyances_Transactions_Undervalue_Final_Report.pdf>.

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[46] The position of the working group is also justified by the fact that a remedy could only be made available in relation to a transaction under which a debtor has in effect converted non-exempt into exempt property by way of a transaction involving the exchange of full or reasonably commensurate consideration by creating a special cause of action that would be limited in application to such transactions. On the view that it is generally undesirable to complicate the statute by attempting to legislate for specific cases, such an approach would not be warranted unless a clear and compelling policy objective exists. The recommendation reflects the fact that the policy rationale justifying an approach that would undermine exemptions law is at least debatable.

[47] The extent to which this approach affects creditors will depend upon the generosity of provincial exemptions law. The working group was cognizant in particular of its implications in the case of a transfer of non-exempt funds into an RRSP that enjoys a full or very liberal exemption. If, for example, a Saskatchewan debtor invests a substantial amount of money in an RRSP in order to shelter assets from creditors the transaction will not give rise to a remedy under the proposed statute because the transaction between the debtor and the financial institution issuing the investment is by definition for full consideration (neither cause of action #1 nor #2 applies), and the institution will not have knowingly participated in a plan to defeat the investor's creditors (cause of action #3 is not available). *[Note: The same result follows in Alberta since RRSPs and other registered plans became exempt under the CEA. Cause of action #1 corresponds with URTA s 7(1)(a), cause of action #2 with s 7(1)(b) and cause of action #3 with s 7(1)(c).]*

[48] The general policy in favour of sheltering RRSPs from creditors is explicitly perpetuated in section 67(1)(b.3) of the BIA except with respect to contributions made during the 12 month period prior to bankruptcy, which may be recovered by the trustee. A roughly similar outcome could be achieved under provincial exemptions law by providing that a debtor may not claim an exemption with respect to funds invested in an RRSP if the debtor was insolvent at the time of the investment, was rendered insolvent by it, or became insolvent within a specified number of days or months after it was made, insolvency being determined on the basis of the value of the debtor's non-exempt assets. The same approach could be applied to any category of exempt property, or exempt property generally. However it was the view of the majority of the working group that any such provision should be considered as a question of exemptions law reform rather than as an aspect of the reform of the general law of fraudulent conveyances.

[49] A final point should be made about the implications of recommendation 2 in relation to a transaction under which a debtor designates a qualifying beneficiary under a policy of insurance with the result that the policy becomes exempt under the provincial Insurance Acts. The definition of transaction gives effect to current case law under which the designation is recognized as the transfer of a property interest to the beneficiary, with the result that such a designation may give rise to a remedy if it falls within any of the causes of action. Most significantly, this means that if the beneficiary has not given consideration, as is usually the case, a remedy will be available if the debtor was insolvent at the time of the designation or made it with the intention of defeating creditors. The remedy granted would in most cases be to set aside the designation, which would avoid the exemption created by the designation and render the policy available to creditors. If this is thought to be objectionable under the exemptions policy effectuated by the Insurance Act legislators may wish to amend those statutes to preclude this result. The working group felt it to be beyond the scope of our mandate to determine exemptions policy by attempting to define a special exception for this unique type of transaction.[61]

7. LIMITATION OF ACTIONS

[87] Proceedings under fraudulent conveyances and fraudulent preferences law are likely subject to the general limitation periods established in the *Limitations Act*.[62] The limitation period prescribed by section 3(1)(a) is 2 years after the date on which the claimant first knew, or in the circumstances ought to have known, that the injury for which a remedial order is sought has occurred and that it warrants bringing a proceeding, or 10 years after the claim arose,

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[61] A policy of insurance by definition includes an annuity contract or insurance policy convertible into an annuity issued by a life insurance company within the scope of the *Insurance Act*. For the relevant provisions, see *Insurance Act*, RSA 2000, ss 637(b), (l), 639, 666(2) and see *Re Klatt*, 2005 ABQB 492 for an explanation of their effect.

[62] *Limitations Act*, RSA 2000, c L-12. The general limitation provision in the Act is apparently intended to include all civil proceedings resulting in a compensatory or remedial order against the defendant or respondent, which would presumably include proceedings under the fraudulent conveyances and fraudulent preferences statutes. However one commentary on the issue suggests that the language of the Act is ambiguous in this context. The argument is that the order granted is not a "remedial order" as defined in section 5 in that it does not require the transferee defendant to comply with a duty or pay damages for violation of a right. See MA Springman et al, *Frauds on Creditors: Fraudulent Conveyances and Preferences*, looseleaf (Toronto: Carswell, 2009) at 5-12 to 5-20. Although the point has not been decided by an Alberta court, the argument was acknowledged by the Alberta Court of Appeal in *Milavsky v Milavsky*, 2011 ABCA 231. The *Limitations Act* replaced the *Limitation of Actions Act*, RSA 1980, c L-15, which clearly included under s 4(1)(g) an action challenging a fraudulent conveyance or fraudulent preference as "any other action not in this Act or any other Act specifically provided for", and it would be surprising if the new Act was intended to remove such proceedings from the scope of the general limitation rule. Any uncertainty would be resolved under the URTA by the limitation provision included in that Act.

whichever period expires first. If this rule were applied to an action under the URTA, the 2 year period would begin to run when a creditor knows or should have known that the debtor has transferred property, performed services, or conferred a benefit in some other form on another person under circumstances that justify an order for relief. The person who has received the property or other benefit could be exposed to an action seeking its recovery *in specie* or in money's worth years after the transaction was concluded, and the period of exposure would vary as among creditors, each of whom may acquire knowledge of the transaction at different times. A transaction that is safe from challenge by Creditor 1, who is well-appraised of the debtor's financial affairs, could be challenged by Creditor 2, who is not.

[88] One of the central motivating policies discussed in Chapter 3 is the need to preserve the finality of transactions and, within reasonable limits, to protect the interests of those who deal with a person who has creditors. Grounds for relief that do not require proof that a debtor intended to obstruct or defeat them will allow creditors to recover more readily than they can under current law, and transferees from an insolvent debtor are commensurately more exposed to an order divesting them of property or exacting monetary compensation for value gratuitously received. This prompted the ULCC working group to recommend that the limitation of action period under the URTA be more restrictive than the general limitation period. The period proposed in section 24 is one year from the date of the transaction or, if the transferee has concealed or assisted in the concealment of the transaction or facts material to the grounds for relief, one year from the date that the person applying for relief knew of the transaction or facts concealed to a maximum of 5 years from the date of the transaction. The limitation of action rules function as a substantive restriction on the grounds for relief rather than as merely a disincentive to tardiness in proceeding. The advantage offered to creditors through the terms of the grounds for relief is counterbalanced in favour of transferees by the limited period during which a transaction is subject to challenge. To quote the working group report, "The 1 year limitation period in effect circumscribes the cause of action and the risk imposed by the law on transferees."[63] The report notes that creditors may be

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[63] Reform of Fraudulent Conveyances and Fraudulent Preferences Law (Transactions at Undervalue and Preferential Transfers), Part 1: Transactions at Undervalue & Fraudulent Transactions, Supplementary Report of the Working Group (Winnipeg 2011), online: Uniform Law Conference of Canada <www.ulcc.ca/images/stories/2011_pdf_en/2011ulcc0005.pdf>.

expected to be reasonably diligent in monitoring debtors' affairs and in pursuing claims.[64]

8. CHOICE OF LAW

[89] The URTA offers a remedy to creditors of a debtor as against a transferee who has received a benefit from the debtor under circumstances that prejudice the creditors' right to enforce their claims against the debtor's property. The Act does not provide a choice of law rule that would determine whether and to what extent the Act applies in a proceeding challenging such a transaction. This is likely to produce significant uncertainty when one or more of the elements of a transaction or dispute are located outside provincial boundaries. A choice of law rule would identify the criterion or criteria that trigger the application of the URTA, as opposed to the law of another other jurisdiction. The question, then, is what basis should be selected. The range of potentially tenable possibilities includes the location of the debtor at the time of the transaction, the law governing the agreement under which the transaction occurred (where an agreement is involved) or the situs of the property or other benefit that was transferred under the transaction.[65]

[90] Although the problem of choice of law may arise under current law, there are no statutory rules or developed jurisprudence guiding its resolution.[66] The approach adopted must therefore be based on an analysis of the relevant factors. Those factors suggest that the location of the debtor at the time of the transaction giving rise to an application for relief is the appropriate criterion.

[91] The first and most important factor to be considered is the nature of the proceeding. The law that permits creditors to seek relief in relation to a

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[64] Reform of Fraudulent Conveyances and Fraudulent Preferences Law (Transactions at Undervalue and Preferential Transfers), Part 1: Transactions at Undervalue & Fraudulent Transactions, Supplementary Report of the Working Group (Winnipeg 2011), online: Uniform Law Conference of Canada <www.ulcc.ca/images/stories/2011_pdf_en/2011ulcc0005.pdf>. The group was asked by the ULCC to reconsider the recommended limitation rules when they were initially presented in the 2010 Final Report on Part I and did so. The recommendation was reaffirmed after careful consideration in the 2011 Supplementary Report on Part I.

[65] The location of the transferee at the time of the transaction or the location of the applicant creditor at the time of the transaction are clearly not worthy of consideration. The rights of creditors should not be determined by the location of an unknown or unknowable potential transferee. Conversely, the rights of a transferee should not be determined by the location of unknown and unknowable creditors. Further, where a debtor has creditors located in more than one jurisdiction a rule based on location of the creditor would make a transaction potentially subject to more than one law.

[66] See MA Springman et al, *Frauds on Creditors: Fraudulent Conveyances and Preferences*, looseleaf (Toronto: Carswell, 2009) at 11-1 *ff.*

transaction that has the effect of defeating or impeding their rights of enforcement against property of a debtor is intimately related to the judgment enforcement system and may be considered an aspect of that system. The claim for relief is based on interference with creditors' existing or prospective right to enforce a judgment. Since any such judgment is a judgment against the defendant-debtor, the focus of enforcement action is the debtor. Once obtained, a judgment will be recognized throughout Canada and, on the authority of the Supreme Court of Canada, may not be challenged on its merits in the jurisdiction in which enforcement is sought.[67] An order made under the URTA by an Alberta court should be respected and enforced by the courts of other provinces and territories under the principles governing the recognition of Canadian judgments.

[92] Secondly, the debtor is the connection between the creditor who applies for relief and the transferee against whom relief is sought; both have dealt with the debtor and the rights and interests of each arise from their respective dealings. People generally are, or certainly should be, alert to the fact that their dealings with others may be affected by the law to which those others are subject by virtue of their residence or location. To put it more concretely, someone who deals with an Alberta resident or a legal entity located in Alberta should recognize that Alberta law defining the rights of that person's creditors is relevant to any dealings with that person. The application of the law of the debtor's location is consistent with the reasonable expectations of those who deal with the debtor, either as creditor or as transferee.

[93] Thirdly, the selection of location of the debtor as the criteria for choice of law recommends itself for lack of a better alternative. A choice of law rule based on the location of the property or other form of benefit transferred under the transaction would be problematic when a transaction involves property located in more than one jurisdiction, services provided in more than one jurisdiction, or some form of property or benefit that does not have an obvious location, such as forgiveness of a debt. A choice of law rule based on the law governing the transaction between debtor and transferee would ignore the nature of the claim as part of the enforcement process and, where the transaction is contractual in nature, may allow the debtor and transferee to thwart creditors' rights of enforcement through a contractual choice of law rule.

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[67] *Morguard Investments Ltd v De Savoye*, [1990] 3 SCR 1077.

[94] Finally, it is worth noting that the Uniform Law Commission of the United States recently approved a choice of law rule in its *Voidable Transactions Act* based on the location of the debtor. The proceedings authorized by the Act are similar in many respects to those falling within Part 2 of the URTA, including in the definition of grounds for relief. The official comment to the enacting provision notes that it provides a simple and predictable choice of law rule applicable to claims for relief of the nature governed by the Act. The comment includes this further observation: [68]

> Basing choice of law on the location of the debtor is analogous to the rule set forth in U.C.C. § 9-301 (2014), which provides that the priority of a security interest in intangible property is generally governed by the local law of the jurisdiction in which the debtor is located.[69] The analogy is apt, because the substantive rules of this Act are a species of priority rule, in that they determine the circumstances in which a debtor's creditors, rather than the debtor's transferee, have superior rights in property transferred by the debtor.

[95] To conclude, the applicable law turns on characterization of the nature of the claim. Since the claim under the URTA relates to enforcement of a judgment, the governing law is properly the law to which the debtor is subject by virtue of his, her or its location. In this context, dealings with a debtor located in Alberta are properly governed by Alberta law and, conversely, dealings with a person located in another jurisdiction are not.

9. OTHER MATTERS

a. Generally

[96] The URTA includes a number of provisions that are not canvassed in this report because they are either relatively minor in terms of policy or largely technical in effect. All are explained in the commentary to the URTA and, aside from the two that are briefly addressed below, warrant no further discussion.

b. The position of secured creditors

[97] The law of fraudulent conveyances and fraudulent preferences is designed to protect unsecured creditors, who have no right of recourse against

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[68] National Conference of Commissioners on Uniform State Laws, *Uniform Voidable Transactions Act* (Formerly Uniform Fraudulent Transfer Act, As Amended in 2014), official comment to s 10.

[69] The same choice of law rule appears in the PPSA, which is Alberta's counterpart to Article 9 of the Uniform Commercial Code. See PPSA s 7(2).

their debtor's property until action is taken through the judgment enforcement system. The law allows them to recover property that would have been available to them under that system, were it not for the debtor's actions. Secured creditors do not need that protection. Their claims are secured by an interest in the debtor's property that follows the property into the hands of a transferee under the principle of *nemo dat* and can be enforced through seizure post-transfer, except where a statutory priority rule intervenes to cut off the creditor's interest or subordinate it to that of the transferee for reasons of policy. While neither the *Fraudulent Conveyances Act, 1571* nor the *Fraudulent Preferences Act* speaks to the rights of secured creditors, relief under both statutes is limited to creditors who are harmed by their debtors' dealings with their property. Since secured creditors are generally able to recover notwithstanding a transfer of the collateral or any other property owned by their debtor, they generally have no claim.

[98] The URTA deals explicitly with the position of secured creditors. Section 3 provides in effect that a secured creditor may only obtain relief under the Act to the extent that the debt owed is unsecured.

[99] Section 4 includes technical rules designed to resolve the complex issues that may arise as a result of the interface between the URTA and the priority rules of the PPSA governing security interests. It resolves any debate over whether creditors may challenge a transfer of property that is subject to a security interest if the security interest is cut off or subordinated in favour of the transferee under a PPSA priority rule. The same question arises in connection with the priority system introduced by the CEA. The issue in that context is whether creditors can challenge a transfer of property that is bound by a registered writ of enforcement if the writ is cut off or subordinated in favour of the transferee under a CEA priority rule. The URTA makes it clear that such a transfer can be challenged. However, where property subject to a security interest is involved, relief is available only to the extent that the property in question would have been available to unsecured creditors acting under the CEA if the transaction had not occurred. A more comprehensive explanation of the rationale for and the operation of the provisions of section 4 is provided in the commentary to the Act.

c. Secondary transferees

[100] Current law does not allow creditors to follow property transferred by a debtor beyond the first transferee. If the person who receives it from the debtor transfers it to a second transferee, the *Fraudulent Preferences Act* allows the

creditors to recover the proceeds or their amount from the first transferee but does not provide for recovery against the second transferee. This means that creditors may be defeated if the property is transferred more than once.

[101] Section 11 of the URTA allows creditors to recover under Part II against a second or subsequent transferee, unless the person against whom relief is sought (a) gave consideration having a value not conspicuously less than the value of the benefit he or she received through the chain of transactions starting with the debtor and (b) does not know that the initial transaction occurred in circumstances that constituted grounds for relief. Section 15 allows creditors to recover under Part III against a second transferee who was not dealing at arm's length with the first creditor or a subsequent transferee who is part of a chain of transactions, each of which was not at arm's length. The BIA similarly allows a trustee to recover property originally transferred under a transaction at undervalue or preferential payment from a secondary transferee, though under somewhat different rules.[70]

[70] BIA, s 98.

CHAPTER 4

Implementing the Uniform Reviewable Transactions Act in Alberta

A. Enactment of the Uniform Reviewable Transaction Act

[102] The Uniform Reviewable Transactions Act should be enacted in Alberta, with such minor revision as may be required to conform to local drafting protocols, to incorporate the few changes suggested below and to appropriately cross-reference Alberta legislation. The Act represents good policy, would strengthen the judgment enforcement system and would greatly clarify the rights of creditors and the corresponding liability of those who deal with a person who has creditors. It is comprehensive in scope and includes rules addressing questions that are either not addressed by current legislation or for which there are no clear answers. It was designed to interface with Alberta legislation governing creditors' rights of enforcement; in particular, with the CEA and the PPSA. The preparation and implementation of an Alberta version of the Act would require a modest investment of government resources and would have little impact on administrative practices within the civil enforcement system.

RECOMMENDATION 1

The Uniform Reviewable Transactions Act should be enacted in Alberta with minor revisions as may be required to: incorporate the changes in the Recommendations in this Report, appropriately cross-reference Alberta legislation and conform to local drafting protocols.

B. Proposed Changes to the Uniform Reviewable Transaction Act

1. MINOR WORDING CHANGES

a. Title of the Act

[103] The title to the legislation as enacted in Alberta would presumably be the *"Reviewable Transactions Act"* without the prefatory *"Uniform"*. However, the abbreviation URTA has been used throughout this discussion for consistency.

b. Definitions

[104] The URTA includes a common law partner within the definition of "spouse." In Alberta, the term "spouse" is reserved for married partners and "adult interdependent partner" is used in place of common law partner. This difference in drafting practice is reflected in the sample draft act.

[105] Similarly, the URTA concept of a "spousal transaction" is a poor fit with Alberta drafting practice. The concept of a spousal transaction is intended to recognize the legitimacy of property transfers to a spouse or adult interdependent partner in the context of a relationship breakdown. The term "separation transaction" is proposed in place of "spousal transaction."

c. Part II title

[106] Part II of the URTA is titled "Transactions at Undervalue and Fraudulent Transactions". The first part of the title accurately reflects the grounds for relief in section 7(1)(a). The second part is intended as a short-hand reference to the grounds for relief in sections 7(1)(b) and (c). Those provisions require proof that the debtor's primary intention in entering into the transaction is "to hinder or defeat the right of a creditor or creditors to recover". The language does not indicate "fraud" or any variant of that word and, as noted in Chapter 3 of this report under heading B, the use of the word "fraudulent" in this context may be misleading. It is recommended that the title to Part II be amended to use the longer but more accurate description, "Transactions at Undervalue and Transactions Intended to Hinder or Defeat Creditors".

2. CLARIFICATION OF SPECIFIC SECTIONS

a. Section 3(1): Application by a secured creditor

[107] The provisions of the Act dealing with the rights of secured creditors are discussed in Chapter 3 under heading D.9.b. The underlying principle is that secured creditors are entitled to relief under the Act only to the extent that their claim is unsecured. This principle is given effect in these words:

> **3(1)** A creditor whose claim is secured by a security interest in property of the debtor may apply for an order for relief under this Act but only with respect to the amount of the claim, if any, that exceeds the value of the property against which the security interest may be enforced.

[108] In its preliminary comments on the potential enactment of legislation based on the URTA, the Legislative Services Branch of the New Brunswick Office of the Attorney General makes this observation in relation to that provision: [71]

> We agree with the premise here – that relief should be available to a secured creditor when direct enforcement against the collateral will be insufficient – but we think the approach should be more flexible. If a secured creditor is not allowed to apply for relief unless the amount of the debt exceeds the value of the property, proceedings could be tied up by preliminary motions dealing with the value of the collateral and the standing of the creditor. It would be better, we think, if any secured creditor could apply for relief, and the court, when determining the remedy, would take into account the extent to which the creditor can recover the debt through direct enforcement.

[109] An arguably better reading is that the provision does not restrict a secured creditor's standing to apply for relief, since it states affirmatively that such a creditor "may apply for an order for relief under this Act". The words that follow qualify the extent of the order for which application is made; the creditor may apply for an order, which shall be framed according to the amount of the claim that is unsecured. On this view, there is no need to determine the extent to which the debt is unsecured to establish the creditor's standing; it is only necessary to determine the extent to which the creditor is entitled to recover from the transferee through any order that might be granted.

[110] However, to avoid doubt and needless litigation, it would be appropriate to clarify the wording of the provision as follows:

> **3**(1) A creditor whose claim is secured by a security interest in property of the debtor may apply for an order for relief under this Act but an order may be granted only with respect to the amount of the claim, if any, that exceeds the value of the property against which the security interest may be enforced.

[111] It is worth noting that the provision, however worded, does two things. It determines the standing of secured creditors and restricts the extent of the order for relief that may be granted to them. While the second dimension of the provision might be more properly located in Part IV, dealing with orders for relief, its placement there might be overlooked. Any restriction on secured creditor's rights should be made clear in the provision determining their standing to apply. Another strategy would be to place the provision determining

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[71] Law Reform Notes #36: December 2014 online: <www2.gnb.ca/content/dam/gnb/Departments/ag-pg/PDF/en/LawReform/Notes36.pdf> at 3 – 4.

standing in section 3 but cast the language of standing "subject to section X", with section X providing a rule restricting the extent of the order and located in Part IV.

RECOMMENDATION 2

Section 3 of the Uniform Reviewable Transactions Act should be revised to make it clear that a secured creditor has standing to apply for relief and that the order for relief granted to a secured creditor is limited to the amount of the claim that is unsecured (i.e., specifically, the amount that exceeds the value of the property against which the claim may be enforced).

b. Section 18(3): Linking the order for relief to civil enforcement distribution rules

[112] Section 18(3) of the URTA recognizes that a creditor who obtains an order for relief under the URTA should be in no better position than he or she would have been in if the challenged transaction had not occurred and the creditor had enforced his or her claim in the usual way through judgment enforcement proceedings against the debtor's property. It requires in general terms that an order for relief be framed in a way that makes the money payable under the order or the value of property affected by the order available to be shared with qualifying creditors of the debtor under the distribution rules of the enacting jurisdiction, which in Alberta are located in the CEA. The commentary to the URTA uses this example to explain the intended result.

> Debtor transfers property to Transferee. Transferee gives no consideration and the circumstances constitute grounds for relief under Part II. Applicant Creditor, whose unsecured claim is worth more than the value of the property, seeks an order against Transferee.

[113] If the transfer had not occurred, the creditor could have had the property in question sold through writ proceedings against the debtor. The proceeds of sale would be a "distributable fund", which would be divided among "eligible claims" under the distribution rules of Part 11 of the CEA. Eligible claims are the amounts outstanding on writs registered against the enforcement debtor when the fund is constituted. The creditor would have been required to share the proceeds of enforcement action with other judgment creditors.

[114] If the creditor in the example were granted relief under the URTA allowing him or her to recover against the property transferred to the transferee or the value of that property, the creditor should similarly be required to share

the fruits of the order with other judgment creditors of the debtor under the distribution scheme of the CEA. Section 18(3) is intended to achieve that result.

[115] Section 18(3) is also designed to ensure that the sharing rules apply as among the creditors of the debtor, not the creditors of the transferee. If the transferee in the example were directed to pay a sum of money, the judgment against the transferee would be enforceable through writ proceedings against him or her and, in the absence of a contrary rule, the fund generated by those proceedings would be shared among those who hold eligible claims against the transferee. The result would be to benefit the creditors of the transferee rather than the creditors of the transferor-debtor.

[116] Section 18(3) as it appears in the URTA is as follows:

> **18**(3) An order for relief must be made in those terms or subject to those conditions that the court considers necessary to make money payable or the value of property to be transferred under the order available for distribution to the persons qualified under *[insert name of province's or territory's creditors' relief statute]* to share in the proceeds of judgment enforcement measures taken against the debtor.

[117] The Alberta statute could use the language of the URTA, inserting the title of the CEA where indicated by the bracketed text. Under that approach, the court would be expected to devise instructions as to how the benefit of the order might be channeled into the CEA distribution regime in a particular case.

[118] Alternatively, additional provisions could be added giving the court more explicit direction. Such provisions might be along the following lines:

> **18**(4) In making an order under subsection 18(3), the court may
>
> (a) order that property owned by a person other than the debtor be sold in writ proceedings and that the proceeds generated by sale of the property be treated as a distributable fund in writ proceedings against the debtor, who shall be named, and distributed under Part 11 of the *Civil Enforcement Act* accordingly,
>
> (b) order that money paid by the transferee under the order for relief be paid to the clerk whereupon it shall be treated as a distributable fund in writ proceedings against the debtor, who shall be named, and distributed under Part 11 of the *Civil Enforcement Act* accordingly,
>
> (c) order that, in the case of writ proceedings taken against the transferee to enforce an order for the payment of money,

> the funds generated by the proceedings shall be treated as a distributable fund in writ proceedings against the debtor, who shall be named, and distributed under Part 11 of the *Civil Enforcement Act* accordingly,
>
> (d) make such other order as may be required.

[119] On balance, it is appropriate to include such a non-exhaustive listing of potential types of order to clarify how the stated objective can be achieved. This clarification would assist not only the court but all parties involved in or contemplating enforcement litigation.

RECOMMENDATION 3

Section 18 of the Uniform Reviewable Transaction Act should refer to the *Civil Enforcement Act* and be expanded to provide more explicit direction as to how the stated objective should be achieved through a non-exhaustive listing of potential types of order.

c. Section 20: Registrations against exempt property

[120] Transactions involving a transfer of exempt property are described in Chapter 3 under heading D.6. As noted there, section 20 applies when a debtor transfers ownership of exempt property to another person but continues to use it for the purpose attracting the exemption. It may be inappropriate to deprive the debtor of the use of the property as an incident of an order for relief against the transferee. The court can respond to that concern by suspending enforcement of an order for relief that would allow creditors to recover the property until such time as it is no longer used by the debtor in the relevant manner. Section 20 contemplates an ancillary order that would prevent the transferee from disposing of the property before the order for relief becomes enforceable. It provides, in general terms designed to accommodate the processes of the enacting jurisdiction, that the court "may order that a [*writ or judgment – depending on the terminology used in provincial judgment enforcement legislation*] be registered against the transferee or the property of the transferee."

[121] As enacted in Alberta, this provision might be better cast in terms of an attachment order rather than a writ. A writ of enforcement is a device for the enforcement of a money judgment under the CEA. It has no function in relation to a judgment declaring an interest in property or any right in relation to property that is not quantified as a monetary claim. An order under section 20 would generally not be cast in terms directing the transferee to pay money, but rather would allow creditors to enforce their claims against the specified

property at some future point in time, to the extent of a prescribed amount. An attachment order would ensure that the property is not disposed of before enforcement action is taken. Like an attachment order granted under the CEA, one granted under section 20 of the URTA could be registered in the *Personal Property Registry* against the name of the person to whom it is directed and under the *Land Titles Act* against the title to land. A registered attachment order has the same priority status as a registered writ. While an attachment order granted under section 20 of the URTA would have the same effect as one granted under the CEA, it differs in that it would be awarded after, rather than in anticipation of, a judgment on the substantive claim. Therefore the provisions of the CEA defining grounds for the award of an attachment order should not apply in this context, nor should many of the related provisions that apply to attachment orders generally.

[122] Section 20 should be clarified to provide that the Court may grant an attachment order where an order for relief in relation to a transaction involving exempt property is suspended until such time as the debtor ceases to use the property in the manner attracting the exemption. Section 20 should also include provisions directing the court as to the terms of an attachment order so granted and should indicate the extent to which the provisions of the CEA that would otherwise govern an attachment order apply.

[123] Accordingly, Section 20 of the URTA could be revised along the following lines:

> 20(1) If an order for relief is granted in relation to a transaction involving exempt property and the debtor continues to use the property in the manner that attracted the exemption, the court
>
> (a) may suspend enforcement of the order for relief until the time that the debtor ceases to use the property in that manner; and
>
> (b) if the enforcement of an order for relief is suspended under clause (a), may grant an attachment order against the transferee.
>
> (2) An attachment order granted under clause (1)(b):
>
> (a) shall direct that the order applies to the exempt property;
>
> (b) may prohibit any dealing with the property or may impose conditions or restrictions on any dealings with the property that may be required to preserve it for purposes of

enforcement of the order for relief at the time referred to in clause (1)(a);

(c) may be registered as provided in section 22 of the *Civil Enforcement Act*;

(d) upon registration under clause (c), has the priority status prescribed in relation to an attachment order by section 23(1) of the *Civil Enforcement Act*.

(3) The provisions of the *Civil Enforcement Act* applicable to attachment orders do not apply to an attachment order granted under this Act, with the exception of paragraph 17(8) of the *Civil Enforcement Act* and the provisions of the Civil Enforcement Act indicated in paragraph (2).

RECOMMENDATION 4

Section 20 of the Uniform Reviewable Transactions Act should be revised to provide that a court may grant an attachment order that may be registered against a transferee or against land affected by the order where the transaction to which the order relates involves exempt property that the debtor continues to use in a manner that attracts the exemption, and should also clarify how the *Civil Enforcement Act* operates in relation to that order.

d. Section 23: Injunctive relief

[124] Section 23 of the URTA authorizes the court to grant injunctive relief against either a debtor or a person who has dealt with or may deal with a debtor in relation to a transaction that has occurred or is reasonably likely to occur. The person subject to an order would be directed not to deal with specified property, or to deal with it only subject to conditions designed to ensure that the property is available to satisfy any order for relief that may be granted if an action under the Act succeeds.

[125] An injunction has only *in personam* effect. A person who violates an injunction by dealing with property contrary to its terms is in contempt of court and liable accordingly, but the property itself cannot be recovered from a *bona fide* transferee. Before the CEA came into effect, prejudgment injunctive orders designed to prevent a defendant from dealing with property in a way that might preclude enforcement of a judgment ultimately obtained in the action, sometimes

called Mareva injunctions, were subject to the limitations of *in personam* effect.[72] The CEA introduced the concept of an attachment order, which fulfils the purpose previously performed by the injunction but has an additional feature. As noted above, an attachment order may be registered and, once registered, the order has a priority status as against a third party who might obtain an interest in the property affected. A registered attachment order has what amounts to *in rem* effect.

[126] Whether it is good policy to encumber a person's property before a substantive claim against them is proven by judgment is a matter of debate.[73] However, that policy has received statutory endorsement under the CEA and the question here is whether it should be extended to proceedings under the URTA. A plaintiff who seeks relief under the URTA would not be entitled to seek an attachment order under the CEA because an attachment order may only be granted in relation to a "claim", which is by definition a claim that may result in a money judgment being granted.[74] Since the form of relief granted under the URTA may be but is not necessarily a money judgment against the transferee, an applicant in a URTA action may not hold a "claim" within the meaning of the CEA.

[127] Section 23 of the URTA could be expanded to allow the court to grant an attachment order in relation to specified property in addition to or in lieu of an injunctive order. If that course were taken, the restrictive conditions governing the grant of an attachment order should apply, as should the other requirements of the CEA generally applicable to attachment orders.[75] Unlike an attachment order granted under section 20, an order under section 23 would be granted before judgment has been granted on the claim for relief. An attachment order could only be granted if the applicant could establish a reasonable likelihood of success in the URTA application, and that there are reasonable grounds to believe that the debtor or the transferee, as the case may be, is dealing with their exigible property otherwise than for ordinary living or business expenses and in

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[72] The practice of writ-saving is an exception. Where a writ has been registered on a default judgment that is set aside to allow trial of the action, the court may order that the writ remain registered pending judgment. The practice has been criticized and it is not clear whether it remains available since enactment of the CEA. See Dunlop & Buckwold, at 233 - 38.

[73] See Dunlop & Buckwold, at 230 - 31.

[74] CEA, s 16(a).

[75] For example, the person who seeks the order must give an undertaking or indemnity against damages caused by the order and may be required to provide security for the undertaking. CEA, s 18(4).

a manner that would likely seriously hinder the enforcement of a judgment obtained in the action.[76]

[128] Extension of the attachment order provisions of the CEA to an order under the URTA would require two steps. First, section 23 of the URTA would require amendment to authorize the court to issue an attachment order in accordance with specified provisions of the CEA in addition to or as an alternative to an injunction. Accordingly, Section 23 of the URTA could be revised along the following lines:

> **23**(1) Whether or not an application for an order for relief has been made, the court may grant an injunction, an attachment order or both to a person who is, or who may become, entitled to apply for an order for relief under this Act if the court is satisfied that there is a reasonable likelihood that a transaction giving rise to a right to relief has occurred or is about to occur.
>
> (2) In granting an injunction, the court may make any orders against the debtor or another person that the court considers necessary to
>
> (a) preserve the benefit of any final order for relief that may be granted;
>
> (b) allow an appropriate order for relief to be made; or
>
> (c) prevent a transaction from occurring.
>
> (3) An attachment order referred to in subsection (1) may be granted against the debtor or another person.
>
> (4) The provisions of the *Civil Enforcement Act* that apply to an attachment order apply to an attachment order granted under this section.

[129] Secondly, a number of the definitions in section 16 of the CEA would require amendment to bring a claim under the URTA within the scope of Part 3. The proposed consequential amendments to CEA section 16 are discussed in the next section.

RECOMMENDATION 5

Section 23 should be amended to authorize the court to issue an attachment order in addition to or as an alternative to an injunction; an attachment order issued under this section should

[76] CEA, s 17(2).

be subject to the provisions of the Civil Enforcement Act governing attachment orders generally

C. Consequential Amendments

1. *BUSINESS CORPORATIONS ACT*

[130] The relief contemplated in relation to a payment of dividends or redemption of its own shares by a corporation is outlined in Chapter 3 under heading D.3. As suggested there, consideration should be given to amending the ABCA to include a corresponding provision that would exempt a corporate director or shareholder from potential liability under both that Act and the URTA in relation to the same payment.

2. CIVIL ENFORCEMENT ACT AND REGULATIONS

a. Section 1

[131] The CEA establishes rules that apply to the seizure and sale of property under "writ proceedings", which are defined as proceedings to enforce a "money judgment". A "money judgment" is defined as one that requires a person to pay money. While an order for relief under the URTA may direct a payment of money, some forms of order will not. For example, the court might order that property involved in a transaction be sold by a civil enforcement agency. The CEA provisions that govern enforcement against property should apply to an order under the URTA, even if the order is not a money judgment. This could be accomplished by amendment of the definitional provisions of the CEA and revision of the form of writ of enforcement.

[132] The definition of "writ proceedings" in section 1(1)(uu) of the CEA should be expanded to include proceedings taken for the purpose of enforcing an order for relief under the URTA, as well as proceedings to enforce a money judgment. In addition, the form of "writ of enforcement" under the CEA should be amended to include an order under the URTA. Once the URTA order is enforceable as a "writ of enforcement", all of the provisions of the CEA that apply to a "writ"would apply to the order, including those relating to registration and priority as well as those governing sale of the property and distribution of the proceeds. Further, the creditor who issues the writ would become an "enforcement creditor" as defined by the CEA and, if that creditor initiates proceedings to enforce the URTA order through sale of the property or

otherwise, the creditor will be the "instructing creditor" and will have the rights and obligations associated with that status.

b. Section 16

[133] As noted above, expanding injunctive relief to include an attachment order under the CEA would require amending a number of the definitions in section 16 of the CEA to bring a claim under the URTA within the scope of Part 3. The amendments should be designed to encompass an order made under the URTA against either the transferee-defendant in the proceedings or the debtor-transferor, who may not be a "defendant" under the current definition. The other CEA provisions applicable to attachment orders should be reviewed to ensure that they operate properly in connection with an order granted under the URTA.

c. Section 96

[134] Section 18 of the URTA is designed to bring any funds generated by an order granted under the Act into the creditor sharing scheme established by the distribution rules in Part 11 of the CEA. The CEA should be amended to facilitate that result. This could be achieved by amending section 96(1) of the CEA to add a further clause along these the lines of clause (c) below:

> **96**(1) All money that
>
> (a) is realized through writ proceedings, or
>
> (b) is otherwise received by an agency as a result of the existence of an enforcement debt,
>
> (c) is received by a distributing authority as a result of an order under the *Reviewable Transactions Act*
>
> must be dealt with in accordance with this Part.

3. REGISTRATION REQUIREMENTS UNDER PPSA AND LAND TITLES ACT

[135] Part IV of the URTA, dealing with orders for relief, includes provisions that contemplate registration in a publicly searchable registry of a security interest created under an order. A "security interest" is by definition an interest in property that secures payment or performance of an obligation.[77]

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[77] URTA, s 1. The definition also includes certain "deemed" security interests for purposes not relevant here.

[136] As noted earlier, a court may frame an order for relief in various ways, including by revesting property in the debtor, in effect reversing the transfer of that property so as to make it available to the debtor's creditors through writ proceedings. This form of order is likely to be rare as the revesting of ownership in the debtor may precipitate the attachment or reattachment of property interests giving rise to difficult questions of priority. The court is more likely to grant a money judgment against the transferee or, if enforcement against the property transferred under the challenged transaction is a better alternative, to order that it be sold in writ proceedings against the transferee. However, there may be cases in which an order vesting the property in the debtor is the best course of action. In an action under Part II (a transaction at undervalue or transaction intended to hinder or defeat creditors), the order may include a provision granting the transferee a security interest in the property to secure the transferee's entitlement to recover the amount of consideration paid for it, or investments made by the transferee that have increased the value of the property.[78] In an action under Part III, the court may grant a security interest to the creditor who received the property in payment of a debt, securing the creditor's recovery of investments that have increased the value of the property.[79]

[137] Section 19(3) provides for registration of a security interest granted under this type of order: in the Personal Property Registry with respect to personal property and in the Land Titles registry with respect to land. The potential for such registrations will require minor amendments to the *Personal Property Security Regulation*, the *Personal Property Security Forms Regulation* and the appropriate provisions of the *Land Titles Act* and *Land Titles Procedures Manual*.

a. Security interests granted in an order for relief under section 19

i. Personal Property Security Forms Regulation

[138] The form of Financing Statement currently used for registration of a security interest under the PPSA indicates a choice of two types of registration; either a PPSA Security Agreement or a *Sale of Goods Act* or *Factors Act* registration. Use of the form for registration of a security interest granted under the URTA will require the addition of a choice designated as "*Reviewable Transactions Act* Security Interest", "*Reviewable Transactions Act* Order", or

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[78] URTA, s 18(4)(b).

[79] URTA, s 18(6).

something to similar effect. Corresponding amendment of the *Personal Property Security Forms Regulation* will be required.[80] The form is otherwise appropriate.

ii. Personal Property Security Regulation

[139] Minor amendments will be required in the *Personal Property Security Regulation*.[81] They include:

- *Secured party*: Section 1(1)(w) "secured party" amended to include a secured party in respect of a security interest granted under the URTA
- *Duration of registration*: Sections 5- 7 amended to indicate the duration of registration of a URTA security interest.
- *Collateral description*: The collateral description indicated in the financing statement should describe the collateral in a manner that is consistent with the terms of the court order and that complies with the ordinary collateral description requirements applicable to security interests. For example, if the court grants a security interest in a boat that is held by the debtor as consumer goods, the financing statement should include the make, model, serial number and collateral category. It may be appropriate to include provisions in Part 4 of the regulations clarifying this point.

iii. Land Titles Act

[140] Two approaches may be considered in relation to registration of a security interest in land granted under a URTA order. The interest might be registered as an instrument under section 122 of the *Land Titles Act* or by caveat under section 130.[82] The better approach would be registration of the security interest as an instrument under section 122 of the *Land Titles Act*.

b. Land Titles Procedures Manual

[141] The Land Titles Procedures Manual should be revised as required to clarify the process for registering a security interest granted under a reviewable transactions order.

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[80] *Personal Property Security Forms Regulations*, Alta Reg 231/2002.

[81] See *Personal Property Security Regulation*, Alta Reg 231/2001, ss 5 - 7.

[82] *Land Titles Act*, RSA 2000, c L-4, ss 122, 130; *Land Titles Forms* Regulations, Alta Reg 480/81, Forms 2.1, 26.

c. Attachment orders granted in an order for relief under section 20

i. Personal Property Security Forms Regulation

[142] The granting and registration of an attachment order either as a form of injunctive relief or under a final order for relief relating to exempt property was discussed above. The form of attachment order currently in use states that it "authorizes enforcement proceedings in accordance with the Civil Enforcement Act." [83] The form would require no modification other than to revise that statement to include an alternative reference to an attachment order issued under the URTA. The *Personal Property Security Forms Regulation* would require a corresponding amendment to include reference to forms prescribed for purposes of the URTA.[84]

ii. Land Titles Act

[143] The current procedure for registration of attachment orders against land should accommodate registration of attachment orders issued under the URTA.

4. RULES OF COURT

[144] The Rules of Court include provisions that may be engaged by litigation under current fraudulent conveyances and fraudulent preferences legislation. The potential need to amend the Rules if the URTA is enacted should be referred to the Rules of Court Committee for its consideration. Points of interface that might be addressed by the Committee include those arising from Rule 9.24 and Rules 13.6 and 13.7.

a. Rule 9.24

[145] Rule 9.24, reproduced below, refers to proceedings under the *Fraudulent Preferences Act*, which will be repealed with enactment of the URTA, and the *Fraudulent Conveyances Act, 1571*, which will no longer apply in the province. Further, the Rule deals with matters that are addressed by the URTA. It may be appropriate to repeal the rule in its entirety if the URTA is enacted.

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[83] *Personal Property Security Forms Regulation*, Alta Reg 231/2002, Form 25.

[84] *Personal Property Security Forms Regulation*, Alta Reg 231/2002, s 1.

Fraudulent preferences and fraudulent conveyances

9.24(1) If a judgment creditor claims to be entitled to relief under the Fraudulent Preferences Act or under the Fraudulent Conveyances Statute, 13 Eliz. I, Chapter 5 (U.K.), on application by the judgment creditor, the Court may order property or part of property to be sold to pay the amount to be collected under a writ of enforcement.

(2) Notice of the application must be served on

(a) the judgment debtor, and

(b) the person to whom it is alleged the property was conveyed.

(3) If a transfer or conveyance is made to defeat, defraud or hinder the rights of a judgment creditor, the judgment creditor, for the purpose of obtaining an order under subrule (1), need not have obtained judgment at the time of the impugned transfer or conveyance.

[146] Subrule (1) presumably refers to a judgment creditor who has obtained judgment and issued a writ of enforcement against a debtor who has transferred property to another person. If the judgment creditor succeeds in challenging the transfer under the *Fraudulent Preferences Act* or the *Fraudulent Conveyances Statute* (i.e. the *Fraudulent Conveyances Act, 1571*), the court may order that the property be sold to satisfy the writ issued against the transferor-debtor. The rule is apparently intended to enable the court to order sale of the property in the hands of the transferee rather than ordering that it revest in the debtor, which would trigger the ordinary CEA rules for enforcement of a writ against the debtor's land. Read broadly, the rule appears to also allow the court to order sale of the land before the plaintiff creditor has obtained judgment in a fraudulent conveyances or fraudulent preferences action. So read, it offers a form of pre-judgment relief in anticipation that the action will succeed and the plaintiff creditor will be entitled to enforce the writ already issued against the debtor-transferor. The URTA includes provisions that deal with both matters. When an applicant creditor succeeds in challenging a transfer of property under the URTA, the court may grant an order for the sale of property in the hands of the transferee.[85] The URTA also makes provision for pre-judgment injunctive relief.[86]

[147] Subrule (3) makes it clear that a creditor need not have a judgment against the debtor at the time a transaction challenged under the *Fraudulent Conveyances*

[85] URTA, s 18(2)(c).

[86] URTA, s 23.

Act or the *Fraudulent Conveyances Act, 1571* occurred. Section 5 of the URTA operates to the same effect.

b. Rules 13.6 - 13.7

[148] Rule 13.6(3) provides that a pleading must:

> ...include a statement of any matter on which a party intends to rely that may take another party by surprise, including, without limitation, any of the following matters:
>
> (d) fraud
>
> (e) illegality or invalidity of a contract, ...

Rule 13.7 requires that a pleading give particulars of fraud included in the pleading.

[149] The grounds for relief under the URTA do not involve proof of fraud, but the historical legacy of the terminology in this area of law may linger. The defendant in an action under the Act might attack the pleadings on the grounds of non-compliance with rules 13.6 and 13.7, obliging the court to determine whether they apply to the URTA action. That eventuality may be avoided by an amendment to the rules explicitly excluding an action under the URTA from their application, or otherwise revising the terms of the rules to address proceedings initiated under the Act.

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MT DUCKETT QC (Vice Chair)

ND BANKES

DR CRANSTON QC

JT EAMON QC

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AL KIRKER QC

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S PETERSSON (Executive Director)

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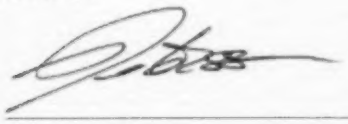
CHAIR



DIRECTOR

APPENDIX A

Uniform Reviewable Transactions Act with Commentary

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This Uniform Act is the product of a joint project between the Law Reform Commission of Saskatchewan and the Uniform Law Conference of Canada

Uniform Reviewable Transactions Act

Introduction

The *Reviewable Transactions Act* replaces the pre-reform statutory and common law that comprised the related branches of law generally referred to jointly as the law of fraudulent conveyances and fraudulent preferences. Like its precursors, the Act is an adjunct to judgment enforcement law and can only be properly understood with an appreciation of that linkage. In this commentary and in the Act, an individual, corporation or other legal person who is subject to a claim that has been or may be reduced to a money judgment is referred to as a debtor. A person who holds such a claim is a creditor. Variants of "he or she" used in the commentary include non-human as well as human creditors and debtors.

A creditor whose claim is secured by a security interest in the debtor's property may take direct action against the collateral to recover the debt. Otherwise, a debt or other claim must be established by obtaining a judgment, which may be enforced in the manner allowed by judgment enforcement law if not voluntarily satisfied. Judgment enforcement law provides the means by which unsecured creditors may recover their claims through seizure or other processes against their debtors' property. The scope and operation of that law varies among jurisdictions but, in principle, it allows for enforcement against any property of the judgment debtor that is not exempt from seizure under provincial or territorial legislation. The reformed systems recently adopted in some provinces are particularly comprehensive and effective. Similar reforms have been proposed in other jurisdictions, generally following the model of the *Uniform Enforcement of Money Judgments Act*.

Unsecured creditors are assured of recovering their claims only to the extent that property of their debtors may be reached through judgment enforcement measures. The law may therefore intervene to protect creditors when a debtor transfers away property or value in another form if the result is to preclude or limit their ability to recover, either by reducing the value of the asset base available through judgment enforcement measures or by creating other obstacles to enforcement. The Act defines the circumstances in which an unsecured creditor is entitled to recover the value lost, and prescribes the type and extent of relief that may be granted.

The Act is organized around a few basic concepts. A transfer of value in any form is a "transaction". The person who benefits under a transaction is the "transferee." The rules of standing and conditions of relief are established by Part II in relation to transactions that are not "creditor transactions" and by Part III in relation to "creditor transactions". Part I applies to proceedings involving a transaction of any kind. Part IV provides for an order

for relief against the transferee, who is required to restore the value lost to the applicant claimant.

The title of Part II indicates two general types of transaction that give rise to a right to apply for relief under that Part. The term "transaction at undervalue" refers to a case in which a debtor who is unable to satisfy unsecured creditors' claims in full transfers property or otherwise gives value to another person for no consideration or for consideration worth conspicuously less than the property or value given. The recipient transferee has received what amounts to a gift at the expense of the debtor's creditors, who are entitled to relief regardless of whether the transaction was deliberately designed to defeat their rights. The term "fraudulent transaction" refers to a case in which a debtor intentionally sets out to hinder or defeat his or her creditors by means of a dealing with property or the conferral of value on another person. Both terms are used descriptively to signal the general scope of Part II but neither appears in the provisions of the Act.

A "creditor transaction" may give rise to relief under Part III. Part III is designed to buttress the creditor sharing rules of provincial and territorial law. In the common law jurisdictions, these rules have existed for more than a century under what is typically called creditors' relief legislation. While the relevant rules vary in scope and detail as among jurisdictions, the basic principle is that a judgment creditor who implements enforcement measures is required to share the funds generated by those measures *pro rata* with other qualifying judgment creditors and, in some instances, with unsecured creditors whose claims are formalized by a certificate or equivalent procedure. The creditor sharing principle is impeded or defeated when a debtor pays one creditor, leaving others unpaid in full or in part and without means to enforce their claims. If the assets of the debtor available under judgment enforcement law are insufficient to satisfy all unsecured creditors, a payment to one or the provision of security for payment is a "preference", since the recipient creditor is preferred relative to other creditors who cannot recover through resort to the debtor's property. The law gives unpaid creditors a remedy as against a preferred creditor in order to ensure that the creditor sharing dimension of judgment enforcement law is not eviscerated through voluntary payments made before a creditor invokes judgment enforcement measures. Part III reflects pre- reform law as well as the preference rules of federal bankruptcy law by offering relief to unpaid creditors in a relatively narrow set of circumstances.

The *Reviewable Transactions Act* does not depart radically in policy and function from the pre-reform law designed to protect unsecured creditors. However, it provides a comprehensive set of clear rules designed to overcome the uncertainty produced by more than a hundred years of incremental legislation and judicial decisions addressed to creditor-defeating dealings. The following passages drawn from the reports on which the Act is based are pertinent:

> The fundamental question that is obscured by current legislation and its judicial interpretation is the wrong at which the law is or should be directed. Is the wrong the *actual* interference with creditors' rights, however laudable the debtor's motives, or only the *intentional* interference with creditors' rights? The difficulty in distilling the answer to this question from the current body of statutory and case law in large part accounts for the uncertainty and inefficiency endemic to its operation.

> [T]he law should be based on the premise that actual interference with creditors' rights of recovery is wrong, except to the extent that countervailing considerations mandate the protection of other legitimate interests. This view does not deny but rather subsumes the proposition that intentional interference with creditors' rights is wrong. Therefore the related policies advanced by our recommendations are the redress of loss occasioned by transactions interfering with creditors' rights of recovery and the deterrence of such transactions so as to forestall the need for redress.
>
> While protection of creditors is a primary focus the rules we advance are designed to appropriately shelter those who deal with debtors by ensuring that they are able to assess and respond to the risk of transacting on the terms proposed or at all.
>
> Any law that subjects a transaction to *ex post facto* challenge necessarily interferes with the finality of transactions to some degree but the potential disruption of settled transactions should be subject to sensible limits. The need to accommodate reasonable reliance on the finality of transactions is recognized as a countervailing policy through various features of the legislation we propose operating in combination...

The definition of predictable outcomes not only simplifies the resolution of disputes when they arise, but diminishes the likelihood that disputes will occur. Debtors, and those who deal with them, are less likely to cross the line between legitimate dealing and creditor avoidance if the line is clearly drawn. Part IV of the Act offers a nuanced and flexible remedial system that facilitates the achievement of fairer outcomes as between creditors and transferees who do engage in transactions that impede creditors' rights in a manner that justifies relief.

The Act advances the harmonization of provincial and territorial reviewable transactions law and the corresponding provisions of the federal *Bankruptcy and Insolvency Act* by adopting some of the same concepts and, in relation to preferential payments, providing rules that produce comparable outcomes.

Some of the provisions of the Act are addressed to concepts, legislation or processes that are part of the law of the common law jurisdictions, as is some of the commentary. For the most part, the Act is suitable for adoption in Québec but adaption of the legislation will be required.

PART I
General

Definitions

1(1) In this Act,

> **"claim"** means the right to satisfaction of an obligation owed by a debtor, whether the obligation is
>
> (a) liquidated or unliquidated,
>
> (b) absolute or contingent,
>
> (c) certain or disputed, or
>
> (d) payable immediately or at a future time;

Comment: The term "claim" is central to the rules that determine standing to apply for relief. A person who holds a claim at the relevant point in time is entitled to apply for relief under section 6 (Part I) or 12 (Part II). The word "obligation" implicitly refers to an obligation enforceable by law through a judgment or order for the payment of money.

A claim must be based on an existing legal obligation, but the obligation need not be immediately enforceable, certain in amount or proven by judgment. An obligation that arises in law from events that have occurred is treated as an obligation owed, even though it may be unliquidated or disputed. For example, a person who has a cause of action against another holds a claim when the actions comprising the cause of action have occurred since the obligation arises from the actions themselves. A typical case is that of a tort victim, who holds an unliquidated claim against the tortfeasor when the tort is committed.

Potential rights against another person that may or may not arise in the future from a judicial order or declaration are not a claim under the Act. A claim may be "contingent" in the sense that performance by the obligor is subject to the fulfillment of a condition, as in the case of a guarantee under which the obligation to pay arises only upon the principal debtor's default. However, the beneficiary creditor holds legally enforceable rights that constitute a claim against the guarantor when the guarantee is given even though the guarantor's obligation may be described as contingent until the conditions that require performance occur. A potential future right to enforce an obligation that does not exist in law until it is declared by the court is not a "contingent" claim in this sense. The position of a person who applies for an order for division of spousal property under provincial or territorial legislation is a case in point. In most jurisdictions, the applicant does not have an interest in the respondent's property and the respondent has no legal obligation to pay money or transfer property until the court makes an order against him or her. In others, legal rights and corresponding obligations arise immediately upon the parties' separation though the court may make an order to determine the means by which those rights are enforced (see *Schreyer v. Schreyer*, 2011 SCC 35). In the first case, a spouse has a potential legal right to payment from the other but the mere status of being a spouse or the fact of having separated does not entail a claim against the other. There is no "right to satisfaction of an obligation" until a court order imposing an obligation is made. A child or spouse who has a potential right to apply for an order for financial support from the estate of his or her deceased parent or spouse under dependants' relief legislation is in a comparable position. (But see s. 6(2) regarding the standing of a person who does not have a claim but has commenced legal proceedings against a debtor.)

"confer" includes to create, grant, provide or transfer;

Comment: The Act applies when a debtor engages in conduct that benefits another person through the conferral of an interest in property or provision of value in another form. The word "confer" denotes whatever legal means of transmission or creation may be involved. For example, a person may "create" a beneficial interest in property through the declaration of a trust, "grant" a security interest or license, "provide" value through the provision of services or forgiveness of a debt, or "transfer" an interest in property. Other forms of the word confer that appear in the Act, such as conferred, confers and conferral, are given corresponding meanings by the *Interpretation Act*.

"creditor" means, subject to section 13, a person who holds a claim;

Comment: The term "creditor" appears in various provisions of the Act but is most significant in connection with the category of transactions defined as creditor transactions. A creditor transaction involves the conferral of a benefit on a person who is a creditor.

"creditor transaction" means a transaction under which a debtor directly or indirectly benefits a creditor by satisfying a claim in whole or in part or by providing security for the satisfaction of a claim in whole or in part but does not include

(a) a transaction under which a debtor

(i) satisfies an obligation that is secured by a security interest in property of the debtor to the extent that the security interest has priority over the rights of unsecured creditors of the debtor,

(ii) confers an interest in property as security for new value advanced by the transferee, or

(iii) gives a security interest in property in substitution for another security interest in property that is of equivalent value and that was given to secure the same obligation, or

(b) a transaction effected

(i) by obtaining or enforcing a court order, or

(ii) by operation of law;

Comment: A creditor transaction is a specific type or subcategory of "transaction", defined below. An application for relief may be made in relation to a creditor transaction under Part III of the Act but not under Part II, except to the extent that the benefit received by the creditor exceeds the value of the creditor's claim (see s.10).

A creditor transaction will ordinarily involve a direct dealing between a debtor and the creditor to whom an obligation is owed. However, a course of action under which a creditor is "indirectly" benefitted by a debtor may also be a creditor transaction. The Act may not be avoided by routing a payment through an intermediate party or otherwise structuring events so that the creditor's claim is satisfied or secured as a result of a debtor's dealing with another person. For example, the payment of a secured debt owed to a senior secured creditor may release that creditor's security interest with the result that the unsecured portion of a debt owed to a junior secured creditor becomes secured. The benefit indirectly received by the junior creditor through enhancement of his or her security originated with the debtor and is a creditor transaction between the debtor and the junior secured creditor (see further comment on s. 1(1) "transaction" clause (k)).

Clause (a) exceptions: A transaction that does not diminish the pool of assets against which creditors may enforce their claims is not objectionable. The exceptions defined by clause (a) ensure that such transactions may not be challenged.

Subclause (a)(i) determines whether a payment to a secured creditor is subject to challenge under Part III as a "creditor transaction". In most cases, payment of a secured debt will discharge the security interest held by the secured creditor, making the newly unencumbered value of the

debtor's property available to satisfy unsecured creditors in lieu of the money or property paid. The rights of unsecured creditors are not affected so the payment is not a creditor transaction. This is not true when unsecured creditors have rights of enforcement that have priority over a security interest discharged by payment. A payment to a secured creditor is therefore exempt from challenge only "to the extent that the security interest has priority over the rights of unsecured creditors."

The question of priority is determined by provincial or territorial judgment enforcement law, supplemented in some jurisdictions by legislation such as the *Personal Property Security Act* or the *Land Titles Act*. Under many statutes, registration of a writ or judgment establishes a priority position for the rights of enforcement associated with the writ or judgment. In other cases, seizure or attachment of property under a writ, judgment or other judgment enforcement device may have priority consequences. The priority status of unsecured creditors relative to secured creditors is determined by (1) whether a step or event that creates a priority status has occurred *(e.g.,.* registration of a judgment or seizure of property) and (2) the operation of a priority rule that applies to the enforcement rights associated with the step or event in question relative to the rights associated with a security interest (*e.g.,* the priority consequence produced by registration or seizure). If no step or event has occurred or no statutory rule gives priority to an unsecured creditor on the basis of such a step or event, a security interest will have priority over the rights of unsecured creditors and a payment to a secured creditor is not a "creditor transaction". If such step or event has occurred and a statutory priority rule gives the rights of enforcement associated with a judgment or writ priority over a secured creditor, a payment to the secured creditor is a creditor transaction.

Example

Debtor grants a security interest in property to Secured Creditor. A writ based on a judgment against Debtor has been registered in accordance with judgment enforcement legislation. The legislation contains a rule that determines priority as between the security interest and the writ on the basis of first to register in the relevant registry. If Secured Creditor registered before the writ was registered, a payment to Secured Creditor is not a "creditor transaction" to the extent of the debt secured and may not be challenged under Part III. If Secured Creditor registered after the writ was registered, a payment to Secured Creditor is a "creditor transaction" that falls within Part III. Unsecured creditors are entitled to satisfaction to the extent of the amount recoverable under the writ before Secured Creditor is paid.

Subclause (a)(ii) recognizes that the conferral of a security interest in exchange for new value does not impinge on the rights of unsecured creditors. While the quality or type of property held by the debtor is altered by the transaction, its total value remains the same. For example, if a debtor borrows $1,000 and grants a security interest in property to secure its repayment, the property interest conveyed to the lender is matched by the money obtained. Since there is no net loss to the debtor's asset base, a transaction under which a debtor gives a security interest for new value is not a "creditor transaction" subject to challenge under Part III. In contrast, when a debtor gives a security interest to secure antecedent (i.e. pre-existing) debt, the effect is to allocate to the benefitting creditor exclusively

property that was available to unsecured creditors collectively; conferral of the security interest is a creditor transaction.

Clause (b) exceptions: Part III of the Act is designed to offer relief when a debtor performs a voluntary action that benefits one creditor, leaving other unsecured creditors unpaid. A creditor who is entitled to recover against a debtor's property under judgment enforcement law, through a right of distress or under another legal process or rule may obtain an advantage relative to other creditors, but the advantage is conferred by the law rather than by the debtor. A transaction effected by obtaining or enforcing a court order or by operation of law is therefore not a "creditor transaction". The creditor sharing principle is not undermined when a creditor recovers a claim through enforcement of a judgment, since judgment enforcement measures engage creditors' relief rules in favour of qualifying unsecured creditors.

"exempt property" means property that is exempt by law from seizure, attachment or any other measure to enforce a money judgment;

"insolvent", with respect to a person, means that

(a) the person is for any reason unable to meet his or her obligations as they generally become payable,

(b) the person has ceased paying his or her obligations in the ordinary course of business as they generally become payable, or

(c) the aggregate of the person's property, other than exempt property, is not, at a fair valuation, sufficient to enable payment of all his or her obligations, whether or not those obligations are currently payable;

Comment: A person whose circumstances fall within any of the three branches of the definition is demonstrably unable or unlikely to pay his or her creditors in full. Therefore, insolvency is a factor in the grounds for relief defined by sections 7 (Part II) and 13 (Part III). Clauses (a) and (b) of the definition exactly parallel the corresponding clauses of the *Bankruptcy and Insolvency Act* (*BIA*) definition of the term. Clause (c) provides a balance sheet test of insolvency, which is designed to determine whether the cumulative value of a person's property is sufficient to satisfy all of his or her financial obligations. The test reflects the equivalent clause of the *BIA* definition but differs in two points of detail. First, only property of a debtor that can be reached by creditors under judgment enforcement law is included in calculating the cumulative value of his or her assets for purposes of determining creditors' rights; exempt property is explicitly excluded. Secondly, the Act resolves a debate about the application of the *BIA* balance sheet test. The issue is whether the calculation of obligations is to take into account only obligations that are currently payable, or all obligations to which a person is currently subject regardless of whether they are payable presently or in the future. The second view is adopted here. The following example illustrates the rationale for this approach.

Example
Debtor has unencumbered non-exempt assets worth $100,000 and owes unsecured debts of $150,000. However, $100,000 of the debt is repayable by instalment over a period of years and Debtor is not currently in default in relation to those payments. Debtor

gives away property worth $50,000 or makes a payment of $50,000 to a non-arm's length creditor. Shortly thereafter, Debtor defaults in paying his or her creditors. The installment debt is accelerated and becomes immediately payable in full.

Under the definition, Debtor was insolvent at the date of the transfer or payment so relief may be available under Part II or Part III, as the case may be. The transferee must restore the $50,000 benefit obtained from Debtor under an order for relief in favour of unsecured creditors. Creditors could not claim relief if the definition of insolvency took into account only obligations that were currently payable at the date of the transaction, unless they could prove the clause 7(1)(a) or subsection 13(1) requirement that Debtor was "demonstrably at risk of insolvency" at the date of the transaction and did become insolvent within 6 months, which may be difficult or impossible.

The valuation of property under clause (c) is not based on the liquidation value that might be obtained in a sale conducted by an authorized official under judgment enforcement measures. The reference to "fair valuation" calls for a valuation based on what the property would be worth if the debtor were to sell it in the conditions prevailing at the relevant time, taking into account circumstances specific to the debtor's business or position.

> **"security interest"** means an interest in property that secures payment or performance of an obligation and, in sections 3 and 4, includes an interest that is a security interest under [*insert section number for PPSA definition relating to leases for a term of more than one year, assignments of accounts and, except in Ontario, commercial consignments*] of the *Personal Property Security Act*;

Comment: This definition adopts what is often referred to as the "substance test" incorporated in the definition of "security interest" found in the *Personal Property Security Acts* (*PPSA*) of the common law jurisdictions. An interest in property given or retained in order to make the property directly available to a creditor for satisfaction of a debt is a "security interest", regardless of the form of the agreement recognizing the interest in question or the legal terminology applied to it. Interpretive guidance may be drawn from the authorities addressing the *PPSA* definition, keeping in mind that the substance test applies in this Act to interests in land as well as in personal property. A mortgagee under a mortgage of land holds a security interest in the land.

The definition also incorporates the interests listed in the extended definition of "security interest" established by the *PPSA* sections indicated, but only in relation to personal property and only for the purposes of the rules in sections 3 and 4 of this Act. The extended definition encompasses interests in personal property that do not secure payment or performance of an obligation and are therefore sometimes referred to as the "deemed" security interests. They are (1) the interest of a lessor of goods under a "lease for a term of more than one year," (2) the interest of the assignee of an account and, (3) in jurisdictions other than Ontario, the interest of a consignor of goods under a "commercial consignment". The *PPSA* definitions for the terms "lease for a term of more than one year", "account" and (other than in Ontario) "commercial consignment" are implicitly incorporated in the *Reviewable Transactions Act* definition, since they give content to the *PPSA* provisions adopted by reference. *PPSA* case law and commentary may

also inform the interpretation of this branch of the *Reviewable Transactions Act* definition.

"separation agreement" means an agreement between a debtor and an individual who is or was the debtor's spouse that

(a) results from or relates to the breakdown of the parties' relationship, and

(b) provides for the division of property and financial resources or for support for the individual who is or was the debtor's spouse or for a member of the debtor's family;

Comment: The term "separation agreement" is a component of the definition of "spousal transaction". Both terms refer to dealings between a debtor and a person who falls under the definition of "spouse".

"spousal transaction" means a transaction in which the parties are or were spouses and that is effected by

(a) a separation agreement, or

(b) a court order for the division of property and financial resources or for support resulting from the breakdown of the parties' relationship;

Comment: A spousal transaction is a particular type of transaction falling within the broader defined category of "transaction". A transaction is a spousal transaction only if it is effected by a separation agreement or by a court order resulting from or relating to the breakdown of the parties' relationship. A transaction between spouses whose relationship remains intact is subject to the rules that apply to transactions generally. Section 14 provides in effect that a spousal transaction that involves the satisfaction of one spouse's claim against the other may not be challenged under Part III as a "creditor transaction," even though it would otherwise fall within the scope of that term. However, relief in relation to such a transaction is not precluded. Subsection 10(2) ensures that relief is available in relation to a spousal transaction under Part II, whether or not the transaction involves satisfaction of or the provision of security for a claim by one spouse against another. The circumstances in which creditors may claim relief in relation to a spousal transaction are limited by subsection 8(2).

"spouse" means an individual who

(a) is married to another individual, or

(b) is cohabiting or has cohabited with another individual as spouses in a [*insert term used in provincial or territorial legislation, such as "spousal", "conjugal" or "marriage-like"*] relationship;

Comment: The definition of "spouse" informs the terms "separation agreement" and "spousal transaction". Persons in a relationship that gives rise to legally recognized rights and obligations approximating those of married persons under the law of the jurisdiction are regarded as spouses for purposes of the provisions of the Act that apply to spousal transactions.

"transaction" means the conferral of a benefit and includes

(a) the conferral of an interest in existing property or property to be acquired in the future, whether or not the property is exempt

property in the hands of the transferor, including a settlement on the transferor as a trustee under a trust,

(b) the provision of services,

(c) the payment of money,

(d) the release of an interest or obligation,

(e) the conferral of a security interest, charge, lien or encumbrance,

(f) the conferral of a licence, quota, right to use or right to payment,

(g) the designation of a beneficiary,

(h) the voluntary purchase or redemption of its shares by a corporation or the voluntary payment of a dividend by a corporation, other than a dividend in the form of its shares,

(i) the refusal by a debtor to act under a power of appointment to confer an interest in property on the debtor,

(j) the disclaimer of an interest in property, whether before or after the interest has vested,

(k) the creation or augmentation of a security interest held by a creditor in property of a debtor as a result of the satisfaction of an obligation owed to another person that is secured by a security interest in the same property if

(i) an unsecured claim of the creditor in that property becomes secured in whole or to a greater extent, or

(ii) a claim of the creditor in that property that was unsecured in part becomes secured in whole or to a greater extent,

(l) the satisfaction of an obligation owed by a person other the debtor,

(m) the conferral of a benefit by a court order or by operation of law;

(n) the assumption of an obligation to do or to bring about in the future any of the events or actions mentioned in clauses (a) to (m);

Comment: The term "transaction" is of central importance in the Act because it defines the foundational requirement for an application for relief. An application may be made under Part II in relation to a transaction that is not a creditor transaction. A "spousal transaction" is subject to Part II but the grounds for relief are narrower than those that apply to transactions generally. An application may be made under Part III in relation to a "creditor transaction." Parts I and Part IV apply to all types of transaction, except as otherwise provided.

Under pre-reform law, only a transfer of property by a debtor could be challenged by creditors as a fraudulent conveyance or fraudulent preference. The definition of "transaction" recognizes that many other actions may directly or indirectly allow a person to acquire or retain value that would otherwise have been available to satisfy creditors' claims. The phrase "conferral of a benefit" encompasses all of the ways in which this may occur.

The enumerated list of actions that constitute a transaction is not exhaustive and most clauses are self-explanatory. A few merit comment.

Clause (a): Clause (a) settles the pre-reform debate over whether a transfer of exempt property is subject to challenge. Relief is available under the Act in relation to any transfer of property, whether or not the property is exempt by law from seizure or other enforcement measures to enforce a money judgment. A debtor who elects to dispose of an exempt asset has implicitly decided that it is not required for the purpose attracting the exemption and is therefore treated by the Act as having surrendered the exemption with respect to that item. The policy and legal obstacles to seizure disappear once the item is no longer used in a manner that justifies protection from creditors and, as between creditors and the transferee, creditors have a higher claim. An order for relief in relation to such a transfer therefore does not undermine the policy of exemptions law. The Act also respects the policy of exemptions law when exempt property is acquired by a debtor in exchange for non- exempt property (see comment on s. 7(1)).

Clause (h): Clause (h) makes it clear that the purchase or redemption of its own shares by a corporation and the payment of a dividend, respectively, constitute a transaction with the recipient shareholder. Subsection 7(2) recognizes that the surrender of purchased or redeemed shares does not added value to the property of the corporation available to satisfy creditors' claims so the corporation is not to be regarded as having received consideration from the shareholder for purposes of determining whether grounds for relief under subsection 7(1) exist.

Clause (k): Clause (k) identifies circumstances that might not otherwise be recognized as a transaction. If a debtor pays a creditor who holds a security interest that has priority over another security interest in the same property, the result may confer a benefit on the subordinate secured creditor through enhancement of that creditor's security. The following examples illustrate the circumstances described by subclauses (i) and (ii) and explain the language used.

> **Example subclause (k)(i)**
> Debtor obtains a loan or credit from secured creditors SC1 and SC2 respectively and enters into a security agreement with each of them. Debtor owes $40,000 to SC1 and $30,000 to SC2. The security agreements give both SC1 and SC2 a security interest in the same property, which is worth $40,000. Since SC1's security interest has priority over SC2's, SC2 is effectively unsecured – i.e. SC1 is entitled to the full value of the property to satisfy his or her debt so if Debtor defaults in paying SC2, SC2 can recover nothing through enforcement against the property.
>
> Assume that Debtor pays $20,000 to SC1. SC1 can claim $20,000 of the $40,000 value of the property to satisfy the debt remaining unpaid but now $20,000 of the value of the property is available to satisfy SC2's claim. The result is that SC2's effectively unsecured claim has become secured in part - i.e. $20,000 of the $30,000 debt is recoverable through enforcement against the property. If Debtor paid out the entire amount owed to SC1, SC2's claim would become fully secured because the property is worth more than the $30,000 debt owed to SC2.

Depending on the conceptual view of SC2's position, the payment results in either "creation" or "augmentation" of a security interest held by SC2 in

property of the debtor as a result of satisfaction of the obligation owed to SC1, which was secured by a security interest in the same property. One view is that SC2 did not have a security interest in the asset before the payment but had a legal right under the security agreement to acquire a security interest that would arise if and when the asset ceased to be fully encumbered by SC1's interest. On that view, the transaction involved "creation" of a security interest held by SC2. Alternatively, SC2 may be regarded as holding a security interest in the asset before the payment to SC1, but the security interest was of no value. Under that theory, the payment to SC1 resulted in "augmentation" of SC2's security interest to the extent of the asset value that became available to SC2. The wording of the definition accommodates either theoretical approach.

> **Example subclause (k)(ii)**
> The facts are the same as in the previous example except that the asset is worth $50,000. In this scenario, SC1's $40,000 debt is fully secured and SC2's $30,000 debt is secured to the extent of $10,000, the remaining value of the property after allocation of $40,000 to SC1. Assume Debtor pays $10,000 to SC1. The result is to "augment" SC2's security interest. In effect, the quantum or value of SC2's interest has grown from $10,000 to $20,000. SC2's claim was originally secured in part, but it has become secured to a greater extent.

In both of the examples given, the "transaction" described by clause (k) is the conferral of a benefit on SC2 as the transferee, not the payment to SC1. The transaction is a "creditor transaction" because the debtor benefited SC2 by providing security for the satisfaction of SC2's claim. The creditor transaction with SC2 may be challenged under Part III if the conditions of relief defined by section 13 are established.

The payment made to SC1 is a transaction between Debtor and SC1 but, while it involved satisfaction of SC1's claim, it is not a "creditor transaction" by virtue of subclause (a)(i) of the definition of that term. An application for relief against SC1 therefore cannot be made under Part III. An order for relief would be available under Part II only in the unlikely event that the conditions of section 7(1)(c) are satisfied. Subsections 7(1)(a) and (b) do not apply when a transferee has given full consideration for the benefit conferred (see comment on ss. 7(1)(a) and (b)).

Clause (l): Clause (l) describes a case in which a debtor pays a debt owed by another person, thereby benefitting that person.

> **Example**
> X owes $10,000 to Y. Debtor pays $10,000 to Y to discharge the debt owed by X.

For purposes of the Act, the example involves two distinct transactions, one under which Debtor benefits Y by the payment and one under which Debtor benefits X by relieving X of the obligation to pay Y. Clause (l) ensures that the conferral of a benefit on X is recognized as a transaction which may be challenged under Part II or, if it was an indirect means of satisfying a debt owed by Debtor to X, as a "creditor transaction" under Part III. The transaction between Debtor and Y is not a creditor transaction because the payment was not made to satisfy an obligation owed by Debtor to Y. Grounds for relief under Part II will exist only in the unlikely event that the circumstances fall within clause 7(1)(c). Relief will not be available under clauses 7(1)(a) or (b) because Debtor received full consideration

from Y (i.e. Y released his or her rights against X in exchange for Debtor's payment).

Clause (m): Clause (m) makes it clear that the conferral of a benefit under a court order or by operation of a rule of law is a transaction. Section 8(3) limits the circumstances in which relief may be granted under Part II in relation to such a transaction. Since a transaction effected by order of the court or by operation of law is excluded from the definition of "creditor transaction", a creditor who obtains a benefit by those means is not subject to an order for relief under Part III.

Clause (n): Clause (n) recognizes that creditors' rights may be threatened when a debtor assumes a present obligation to confer value in the future. An "obligation" is an obligation enforceable by law. An injunctive order may be the appropriate form of relief in such a case.

> **"transferee"** means a person who benefits under a transaction and includes a creditor who benefits under a creditor transaction.

Comment: When grounds for relief are established, the order for relief is made against the transferee, not the debtor. The objective is to restore value to the creditors to whom it was lost by means of the transaction or, through the issuance of an injunction, to prevent a transferee from receiving value to which creditors are entitled. In most cases, the benefit will be received directly from a debtor. However, a benefit may be conferred indirectly, as in the cases contemplated by clauses (k) and (l). For the purposes of the Act, a person who receives an indirect benefit is the transferee in a transaction with the debtor.

(2) A transaction may be a single event or may comprise a series of closely related events, including the provision of services over time.

Comment: Subsection 1(2) recognizes that the incremental or episodic conferral of a benefit over a period of time may comprise one transaction. The stipulation that a transaction may comprise a series of "closely related events" is designed to differentiate a single transaction spread over time from a succession of discrete events, each of which is a separate transaction. While there is no bright line test, the phrase should be interpreted in light of the objectives of the Act taking into account the consequences of alternative characterizations from the perspective of the transferee, whose liability may be determined by the conclusion reached. The question of whether multiple events constitute a single transaction or a series of transactions is particularly significant in relation to the limitation of actions rules that run from the date of a transaction (see s. 24). When successive events are not closely related, the limitation period applicable to the first is calculated from the date it occurs, not from the date of the last event.

(3) The date of a transaction is the date on which a benefit is conferred and, if the transaction comprises a series of closely related events, the date when the events are substantially completed.

Comment: The date of a transaction comprised of a series of closely related events is the date when the events are substantially completed, which will ordinarily be the date on which the last event occurs. However, a transaction may be substantially complete even though something inconsequential remains to be done.

(4) For the purposes of this Act,

(a) an individual has knowledge when the relevant information is acquired by the individual under circumstances in which a reasonable person would take cognizance of it;

(b) a partnership has knowledge when the relevant information comes to the attention of one of the general partners or a person having control or management of the partnership business under circumstances in which a reasonable person would take cognizance of it;

(c) a corporation has knowledge when

(i) the relevant information comes to the attention of

(A) a managing director or officer of the corporation under circumstances in which a reasonable person would take cognizance of it, or

[*Alternative language to corresponding effect may be used in jurisdictions that do not recognize the office of "managing director" in corporation law.*]

(B) a senior employee of the corporation with responsibility for the matter to which the information relates under circumstances in which a reasonable person would take cognizance of it, or

(ii) the relevant information in writing is delivered to the corporation's registered office or attorney for service;

(d) the members of an association have knowledge when the relevant information comes to the attention of

(i) a managing director or officer of the association under circumstances in which a reasonable person would take cognizance of it,

(ii) a senior employee of the association with responsibility for matters to which the information relates under circumstances in which a reasonable person would take cognizance of it, or

(iii) all members under circumstances in which a reasonable person would take cognizance of it; and

(e) a government has knowledge when the relevant information comes to the attention of a senior employee of the government with responsibility for the matter to which the information relates under circumstances in which a reasonable person would take cognizance of it.

Comment: Subsection 1(4) defines the circumstances that constitute knowledge or the state of knowing for purposes of the Act. Interpretive guidance may be drawn from case law and commentary addressing the substantially similar rules that appear in the *Personal Property Security Acts* of the common law jurisdictions and, in some jurisdictions, the reformed judgment enforcement legislation. A person who subjectively knows something clearly has knowledge. Under the "constructive knowledge" rules incorporated in these provisions, a person who has information about the fact in question is deemed to know it if the circumstances are such that a reasonable person would have taken cognizance of the information. A person who actively avoids information that would give rise to actual or constructive knowledge should not be permitted to circumvent legal consequences on the

grounds that the information avoided is lacking; wilful blindness is not a defence.

Applications for relief to be made to [superior court of jurisdiction]

2 All applications for an order for relief under this Act must be made to [*superior court of jurisdiction*].

Rights of secured creditors

3(1) A creditor whose claim is secured by a security interest in property of the debtor may apply for an order for relief under this Act but only with respect to the amount of the claim, if any, that exceeds the value of the property against which the security interest may be enforced.

Comment: The Act is designed to provide a remedy to unsecured creditors whose ability to enforce their claims against their debtor's property under the judgment enforcement system is defeated or impeded by the alienation of value that would otherwise have enhanced the pool of assets available to them. The transferee is obliged to restore the value lost. A creditor who holds a security interest in the debtor's property may enforce that interest through sale or collection of the subject property or by means of foreclosure. Secured creditors are therefore not entitled to relief under the Act to the extent of the value of the property against which the security interest may be enforced. However, any amount of the debt that exceeds that value is effectively unsecured and may be recovered only through the judgment enforcement system. While a secured creditor may not apply for relief in relation to the secured portion of the debt, he or she is treated as an unsecured creditor for purposes of the Act to the extent of any unsecured amount.

The word "enforced" as it is used in subsection 3(1) refers to the creditor's ability to recover the debt in relation to which the security interest is given through realization against property subject to that interest. The typical case in which a claim "exceeds the value of the property against which the security interest may be enforced" is one in which the debt owed is greater than the value of the asset or pool of assets subject to the security interest. If the debt is $50,000 and the collateral is worth $40,000, the secured creditor is in the same position as an unsecured creditor who is owed $10,000. Subsection 3(1) also applies to the less obvious case of a subordinate secured creditor, who is entitled to relief under the Act to the extent that his or her ability to enforce the security interest is precluded by the rights of the secured creditor whose interest has priority. The following example illustrates this feature of the rule.

> **Example**
> Debtor owes $30,000 to Secured Creditor 1 (SC1) and $20,000 to Secured Creditor 2 (SC2). Both secured creditors hold a security interest in an asset worth $40,000. The security interest held by SC1 has priority over that held by SC2. Although the debt owed to SC2 is less than the value of the collateral, SC2's ability to enforce his or her security interest is limited by the rights of SC1. Only $10,000 of the $40,000 collateral value is available to SC2, who is effectively unsecured to the extent of $10,000. SC2 is entitled to relief under the Act to the extent of the unsecured debt.

(2) If a debtor transfers property that is subject to a security interest and another Act provides that the security interest is subordinated to the interest of the transferee or that the transferee takes the property free of the security interest,

(a) the property is not to be considered property against which the security interest may be enforced for the purposes of subsection (1) in proceedings relating to that transfer or to another transaction; and

(b) if an order for relief is made under this Act in relation to the property transferred, whether in proceedings by the creditor or by another person, the creditor may not assert a claim to the property on the basis of the security interest.

Comment: A secured creditor is able to rely on his or her security interest to recover the secured debt only so long as that interest survives and is enforceable against the collateral. When a debtor transfers property subject to a security interest to another person, a priority rule provided by the *Personal Property Security Act*, the *Land Titles Act* or other legislation may either eliminate the security interest or subordinate it to the interest of the transferee. For example, some *PPSA* rules provide that a transferee of personal property "takes free of" a security interest in the property under prescribed circumstances. Some provide that the security interest is "subordinate to" the interest of the transferee. Other statutes may contain priority rules that produce one result or the other without using that language. In all such cases, the security interest can no longer be enforced against the property in the hands of the transferee. Clause 3(2)(a) makes it clear that if a debtor transfers property in circumstances that fall within a priority rule of this kind, the property transferred is not to be taken into account in determining whether the secured creditor is entitled to relief under the Act. The creditor is in the same position as an unsecured creditor to the extent that his or her claim has become effectively unsecured as a result of the operation of the priority rule.

Example 1
Secured Creditor holds a security interest in a car owned by Debtor to secure recovery of a $20,000 debt. Secured Creditor has not taken the steps required to "perfect" the security interest under the *PPSA*. Debtor sells the car to Transferee. A *PPSA* priority rule provides that the security interest is subordinate to the interest of Transferee, so it can no longer be enforced against the car. Since the car is not to be considered property against which the security interest may be enforced for the purposes of subsection 3(1), Secured Creditor may claim relief under the Act as the holder of an unsecured $20,000 claim.

Example 2
The facts are the same as in Example 1, but Secured Creditor also has a security interest in a truck owned by Debtor to secure recovery of the
$20,000 debt. The truck is worth more than $20,000. Although the value of the car has been lost to Secured Creditor as a result of the priority rule triggered by the sale to Transferee, Secured Creditor is not entitled to claim relief under section 3(1) because his or her claim does not exceed the value of the property against which the security interest may be enforced, namely, the truck.

Clause 3(2)(a) applies if proceedings are taken to challenge the transaction under which property subject to the security interest in question is transferred away by the debtor. However, it is more likely to be relevant in proceedings taken in relation to another transaction entered into by the debtor. To use the facts of Example 1, Secured Creditor has become

effectively unsecured by sale of the car and is treated as an unsecured creditor for purposes of the right to relief under the Act. If Debtor gives another asset to Transferee or to another person in a separate transaction, Secured Creditor is entitled to apply for relief under the Act in relation to that transaction. Secured Creditor is treated as an unsecured creditor for purposes of the proceedings.

Clause 3(2)(b) forestalls any argument that a secured creditor whose security interest is eliminated or subordinated due to the operation of a priority rule is restored to his or her original position if an order is granted under Part IV revesting the property transferred in the debtor. A secured creditor cannot assert the rights of an unsecured creditor in proceedings to challenge a transfer of property and then reclaim the status of secured creditor when the proceedings succeed, thereby reversing the operation of the priority rule.

Example 3
Secured Creditor holds a security interest in an asset owned by Debtor. Debtor transfers the asset to Transferee under circumstances that trigger a priority rule that allows Transferee to acquire it free of the security interest. Secured Creditor or another creditor seeks an order for relief in relation to the transaction and the court grants an order revesting the asset in Debtor so it can be reached by the applicant under judgment enforcement measures. Secured Creditor cannot claim that his or her security interest reattaches and can be enforced against the asset when it revests in Debtor. Secured Creditor has the rights of an unsecured creditor, which may entail a right or an obligation to share with other unsecured creditors under creditors' relief law.

There will be very few cases in which a transfer of property that triggers a priority rule in favour of the transferee involves circumstances that constitute grounds for relief under this Act. Section 3(2)(b) clarifies the outcome in that rare case.

The extended definition of "security interest" applies to Section 3 (see s. 1(1) "security interest" and comment). If the property in the examples above were goods held by the debtor under a lease for a term of more than one year within the meaning of the *PPSA*, the lessor would be in the position of Secured Creditor with respect to his or her "deemed" security interest in the goods.

Relief where transaction involves property subject to a security interest or [writ, enforcement charge or judgment, depending on the legislation of the enacting jurisdiction]

4(1) An application for an order for relief may be made in relation to a transaction that involves property that is subject to a security interest or a [*writ, enforcement charge or judgment, depending on the legislation of the enacting jurisdiction*] even if under another Act

(a) the security interest or the [*writ, enforcement charge or judgment*] is subordinated to the interest of the transferee; or

(b) the transferee takes the property free of the security interest or [*writ, enforcement charge or judgment*].

Comment: Section 4 differs in scope from section 3, though some circumstances will invoke both. Section 3 defines the rights of secured creditors in relation to transactions entered into by their debtors,

regardless of whether the proceedings relate to a transaction that involves the property subject to the security interest. A secured creditor has the rights of an unsecured creditor to the extent that the debt cannot be recovered through enforcement of the security interest (see comment on s. 3). Section 4 applies to transactions that involve a transfer of property that is subject to a security interest or to the rights of judgment creditors established through the means offered by the judgment enforcement law of the jurisdiction. Section 4 determines the availability of relief when such a transaction is challenged by any creditor. A "security interest" within the meaning of this section includes a "deemed" security interest encompassed by the extended definition of the term (see s. 1(1) "security interest" and comment).

The rights of secured creditors differ conceptually and functionally from those of judgment creditors, but they are comparable in that both entail a right to satisfaction of a debt through enforcement against or appropriation of the debtor's property in the manner permitted by law. In both instances, the rights of enforcement have a priority status relative to competing interests in or claims to the property. The determination of priority in relation to the rights of judgment creditors depends upon the type of enforcement mechanism used in a given jurisdiction and the steps that must be taken to establish a status that has priority implications. In some jurisdictions, judgments may be enforced through a writ of execution, a writ of enforcement, garnishee summons or similar device while in others a judgment is enforceable without an interstitial formality or process if prescribed steps are taken. The term "enforcement device" is used here generically to include all such approaches.

When a debtor transfers away property that is subject to a security interest, the transferee ordinarily acquires the property subject to that interest. However, a security interest may be eliminated or subordinated to the rights of the transferee under a statutory priority rule found in the *Personal Property Security Act* or *Land Titles Act* of a common law jurisdiction (see comment on section 3) or in other legislation. Similarly, priority rules exist under judgment enforcement legislation in relation to whatever enforcement device is used to establish the priority of judgment enforcement rights. Under many systems, the priority of the enforcement device depends on registration of a judgment or writ in a public registry. In some cases, priority is based on seizure or attachment of the debtor's property. Those who acquire an interest in a property that is subject to a judgment enforcement device generally take subject to the rights of judgment creditors but, as with security interests, exceptions may be created by a priority rule. In jurisdictions that have reformed their judgment enforcement legislation, the priority rules that apply to a judgment enforcement device affecting personal property roughly parallel those that apply to a security interest in the same type of property. A transferee of property from the judgment debtor may acquire it free of the rights of judgment creditors associated with the enforcement device, or those rights may be subordinated to the interest of the transferee. The fact that a transferee takes free of a security interest or enforcement device or has priority under a statutory rule does not preclude an order for relief. This approach is justified by the fact that priority rules serve a limited purpose within the confines of the statute in which they are located and do not override rights offered by other statutes or rules of law. In practice, a transaction that invokes a priority rule in favour of the transferee will rarely involve circumstances that constitute grounds for relief under the Act.

(2) If a transaction involves property that is subject to a security interest at the date of the transaction, an order for relief may be made only if the transaction reduces the amount or value of property that would have been available to unsecured creditors under judgment enforcement measures if the transaction had not occurred.

Comment: The Act is designed to provide relief to unsecured creditors when property against which they might have enforced their claims is lost through a transaction entered into by their debtors. Unsecured creditors are not affected if a transaction involves property that is subject to a security interest that has priority over any rights they might be entitled to assert against that property under a judgment enforcement device. The effect of subsection 4(2) is to limit or preclude an order for relief if the transaction does not reduce the amount or value of property that would have been available under judgment enforcement measures. If a security interest that has priority over the rights of unsecured creditors secures a debt in an amount less than the value of the property transferred, unsecured creditors are entitled to relief to the extent of the surplus value lost to them as a result of the transaction. Conversely, if a judgment enforcement device has priority over a security interest to the extent of an amount less than the value of the property, relief is available to the extent of that amount but not for the full value of the property. Only the amount that could have been recovered by judgment creditors if the transaction had not occurred is recoverable under the Act.

The following examples illustrate the operation of subsection 4(2).

Example 1: security interest has priority

Debtor owns an asset that is subject to a security interest held by Secured Creditor. A judgment enforcement device (*e.g.*, a writ or judgment) has been registered against Debtor or against the asset, as the case may be. The security interest has priority over the judgment enforcement device under judgment enforcement legislation or another applicable statute (*e.g.*, because it was registered first). Debtor transfers the asset to Transferee in circumstances that constitute grounds for relief under the Act.

Variation A

The asset is worth $30,000 and Secured Creditor is owed $35,000. Unsecured creditors could not have recovered their claims through seizure of the asset under a judgment enforcement measure if it had not been transferred to Transferee because the full value of the asset is encumbered by the security interest. An order for relief may not be made under the Act because unsecured creditors' rights of recovery are not affected by the transaction.

Variation B

The asset is worth $30,000 and Secured Creditor is owed $10,000. Unsecured creditors could have recovered their claims through seizure of the asset under judgment enforcement measures to the extent of $20,000 if it had not been transferred to Transferee. Since recovery is limited but not precluded by the security interest, relief is available against the transferee to the extent of the $20,000 value lost as a result of the transaction.

Example 2: security interest is subordinate
Debtor owns an asset that is subject to a security interest held by Secured Creditor. A judgment enforcement device (*e.g.* a writ or judgment) has been registered against Debtor or against the asset, as the case may be. The security interest is subordinate to the judgment enforcement device under judgment enforcement legislation or another applicable statute (*e.g.* because the judgment enforcement device was registered first). Debtor transfers the asset to Transferee in circumstances that constitute grounds for relief under the Act.

Variation A

The asset is worth $30,000 and the judgment enforcement device is based on a judgment in the amount of $35,000. Unsecured creditors could have recovered their claims through seizure of the asset under a judgment enforcement measure in spite of the security interest if it had not been transferred to Transferee. An order for relief may be made under the Act because alienation of the asset reduces the amount or value of property that would have been available under judgment enforcement measures if the transaction had not occurred.

Variation B

The asset is worth $30,000 and the judgment enforcement device is based on a judgment in the amount of $10,000. Unsecured creditors could have recovered their claims through seizure of the asset under judgment enforcement measures to the extent of $10,000 if it had not been transferred to Transferee. If the amount owed to Secured Creditor is more than the remaining $20,000 value of the asset, unsecured creditors are not entitled to recover against that value even if additional but subordinate judgment enforcement devices exist in relation to other judgments. An order for relief may be made under the Act to the extent of the $10,000 value that would have been available under judgment enforcement measures if the transaction had not occurred.

(3) In determining under subsection (2) whether or not property would have been available to unsecured creditors under judgment enforcement measures if the transaction had not occurred,

(a) no regard is to be had to whether or not the property is or was exempt property; and

(b) if the security interest is subordinated to the interest of the transferee or the transferee takes free of the security interest, the security interest is to be considered unenforceable against unsecured creditors.

Comment: Subsection 4(3) responds to two factors that may affect the operation of section 4(2). Clause 4(3)(a) deals with a transfer of exempt property. Since exempt property cannot be reached under judgment enforcement measures while it remains in the hands of the debtor, a transfer of exempt property does not "reduce the amount or value of property that would have been available to unsecured creditors under

judgment enforcement measures if the transfer had not occurred." However, the Act adopts the general policy that a transfer of exempt property is not immune from challenge (see comment on subsection 1(1) "transaction"). The debtor is treated as having surrendered the exemption. If relief is available in relation to a transfer of exempt property that is not subject to a security interest it should similarly be available in relation to a transfer of property that is. Clause 4(3)(a) achieves that result. If a transaction involves a transfer of exempt property, the property is to be treated as if it were not exempt for purposes of the rule in subsection 4(2).

Clause 4(3)(b) deals with a transfer of property that is subject to a security interest that is eliminated or subordinated to the transferee under a priority rule contained in legislation such as the *Personal Property Security Act* of a common law jurisdiction (see comment on s. 3). Subsection 3(2) recognizes that the holder of the security interest has become effectively unsecured and allows him or her to challenge that transaction or another transaction entered into by the debtor on the same basis as any unsecured claimant. Clause 4(3)(b) qualifies the operation of subsection 4(2) in such a case. The property transferred is to be treated as if the security interest were unenforceable against unsecured creditors before the transfer occurred, making it available under judgment enforcement measures for the purposes of subsection 4(2).

The combined effect of subsections 4(3)(b) and 3(2) may be demonstrated by reference to Example 1 in the comment on subsection 4(2). If Transferee takes free of Secured Creditor's security interest, Secured Creditor is treated as the holder of an unsecured claim for purposes of the right to relief under the Act. There will be few cases in which a transaction that attracts the operation of a priority rule in favour of the transferee involves circumstances constituting grounds for relief. However if grounds are established, the formerly secured party or any other unsecured claimant may seek an order for relief even though the property would not have been available to unsecured creditors under judgment enforcement measures if the transaction had not occurred due to the pre-transfer status of the security interest. The security interest is treated as if it were unenforceable against unsecured creditors for the purposes of determining the availability of relief under the Act.

When applications for orders of relief may be made and claims may be established

5(1) An application for an order for relief under this Act may be made whether ornot the person who applies for relief has commenced proceedings or obtained a judgment against the debtor in relation to a claim.

(2) A person who applies for an order for relief under this Act is entitled to a benefit under an order for relief only if a judgment has been granted against the debtor on the person's claim.

(3) If a person does not have a judgment against the debtor in relation to a claim,

(a) the person may make the debtor a defendant in the proceedings and the court may

(i) grant judgment against the debtor for the amount of the claim that is proven in the proceedings or that is not contested by the debtor, or

(ii) direct a separate trial to determine the validity and amount of the claim; and

(b) the court may

(i) stay the proceedings or suspend the operation of an order for relief until a judgment is obtained either as part of the proceedings related to the application for relief or in another action, and

(ii) make any supplementary orders that the court considers appropriate.

Comment: A person has standing to apply for relief under the Act if he or she holds a claim against the debtor who engaged in the transaction that is the subject of the application (see ss. 6 in Part II and 12 in Part III). Subsection 5(1) makes it clear that a person who has standing may commence proceedings under the Act regardless of whether judgment has issued on his or her claim. However, subsection 5(2) requires an applicant to prove his or her claim by obtaining judgment against the debtor before he or she can benefit under an order for relief against the transferee.

Subsection 5(3) enables the court to manage the proceedings in whatever fashion may be appropriate to ensure that a claim against the debtor is established while protecting the applicant's potential right to relief under the Act until it is. A stay of proceedings is likely to be granted if the material before the court indicates that the applicant's claim is doubtful. The transferee should not be forced to defend an application for relief in those circumstances. If an order for relief is suspended or a stay of proceedings granted, the court may make such orders as may be required to preserve the property required to satisfy the existing or potential order for relief. Section 23 provides for the issuance of an injunction.

Some or all of the rules provided in subsection 5(3) may be omitted from the Act if the law of the enacting jurisdiction empowers the court to make orders and issue directions of the kind contemplated.

PART II
Transactions at Undervalue and Fraudulent Transactions

Introductory comment: The function of Part II is described in summary fashion in the introduction to the Act. It offers relief if a transaction prevents unsecured creditors from recovering their claims through enforcement against property of the debtor that would otherwise have been available to them, or if a transaction materially hinders their recovery. Section 6 identifies the persons who have standing to apply for relief and section 11 identifies those against whom relief may be granted. Sections 7, 8 and 9 define the circumstances in which relief is available. Section 10 deals with the relationship between Parts II and III. The terms of the order for relief are determined by Part IV. The provisions of Part I also apply to an application under Part II.

Who may apply for order of relief under this Part

6(1) An application for an order for relief under this Part may be made by

(a) a person who holds a claim that existed at the date of the transaction that is the subject of the application for relief; and

(b) in the case of relief claimed on the grounds of relief mentioned in clause 7(1)(b) or (c), a person who holds a claim that arose after the date of the transaction that is the subject of the application for relief.

(2) For the purposes of permitting an application for relief to be made under this section

(a) a person who has commenced legal proceedings seeking an interest in the property of a debtor or an order for the payment of money against a debtor is to be regarded as a person who holds a claim; and

(b) a person who is a defendant in the legal proceedings mentioned in clause (a) is to be regarded as a debtor whether or not a judgment has been granted against that person at the time the application is made.

Comment: Section 6 provides the rules that determine whether a person has standing to apply for relief in relation to a transaction that involves circumstances constituting grounds for relief under Part II. The date of a transaction is determined in accordance with subsection 1(3). Clause 6(1)(b) recognizes that relief should be available in some circumstances to a person who did not hold a claim at the date of a transaction but whose claim could be anticipated. A person who acquires a claim after a transaction has occurred may apply for relief only on the grounds specified in clauses 7(1)(b) or (c). Proceedings by a person whose claim arises more than 1 year after the date of a transaction will be barred by the limitation of actions rules in section 24.

A person has a "claim" as defined in the Act only if he or she is entitled to satisfaction of an obligation owed by a debtor. Subsection 6(2) is addressed to a case in which a person may take legal action against another but any obligation owed by the defendant will arise only if an order is made against him or her by the court (see comment on subsection 1(1) "claim"). Without special provision, the person who commences the action would not have standing to challenge a transfer of property or other transaction by the defendant if the transaction occurs before judgment issues in the underlying litigation. Subsection 6(2) allows a person who has commenced legal proceedings seeking an interest in property or a money judgment to seek relief under clause 6(1)(a) in relation to a transaction that occurs after those proceedings are commenced. If the litigation is launched after a transaction occurs, the plaintiff has standing under the terms of clause 6(1)(b). Clause 6(2)(b) deems the defendant in the proceedings described in clause (a) to be a debtor even though an order giving rise to an obligation to the applicant has not been made.

A person who has standing under section 6 may be prevented by other provisions from obtaining relief. Section 3 precludes an order for relief in favour of a creditor whose claim is fully secured. Subsection 4(2) may bar or limit an order for relief in favour of any claimant if a transaction involves a transfer of property that is subject to a security interest. Section 5 prevents a person who has standing from benefiting under an order for relief against a transferee without proving his or her claim against the debtor through procurement of a judgment.

Grounds for relief under this Part - transactions at undervalue or fraudulent transactions

7(1) Except as otherwise provided in this Act, an order for relief may be made under this Part

(a) in relation to a transaction in which the debtor receives no consideration or consideration worth conspicuously less than the value conferred by the debtor under the transaction, if the debtor

(i) is insolvent at the time of the transaction,

(ii) becomes insolvent as a result of the transaction, or

(iii) enters into the transaction in circumstances in which the debtor is demonstrably at risk of insolvency and the debtor becomes insolvent within 6 months after the date of the transaction;

(b) in relation to a transaction in which the debtor's primary intention is to hinder or defeat the right of a creditor or creditors to recover in whole or in part claims that, at the time of the transaction, were existing or were reasonably foreseeable, if

(i) the ability of the creditor or creditors to recover their claims is materially hindered as a result of the transaction, and

(ii) the debtor receives no consideration or consideration worth conspicuously less than the value conferred by the debtor under the transaction; or

(c) in relation to a transaction in which the debtor's primary intention is to hinder or defeat the right of a creditor or creditors to recover in whole or in part claims that, at the time of the transaction, were existing or were reasonably foreseeable, if

(i) the ability of the creditor or creditors to recover their claims is materially hindered as a result of the transaction, and

(ii) the transferee knew of the debtor's intention and intended to assist the debtor by entering into the transaction.

Comment: Clauses (a), (b) and (c) of subsection 7(1) define three sets of conditions that constitute grounds for relief under Part II against a transferee who has benefitted under a transaction with a debtor. Any of the three is generally available to a person who holds a claim at the date of the transaction, including a person described in clause 6(2)(a). An applicant whose claim arises after a transaction occurs is prevented by clause 6(1)(b) from claiming relief under clause 7(1)(a). Only a transferee who benefits under a transaction that was intended to hinder or defeat the rights of a creditor within the meaning of clauses (b) or (c) is liable to a post-transaction claimant. The availability of relief is also restricted in relation to certain types of transaction by section 8. Section 10 provides that relief is available in relation to a creditor transaction only under Part III, except to the extent provided. Section 9 provides grounds for relief that are uniquely available in relation to transactions involving payments by corporations that do not fall within section 7.

A person who seeks relief under any of the causes of action defined by subsection 7(1) must establish that a debtor participated in a "transaction" which, by definition, involves the conferral of a benefit on a transferee. The term "debtor" is not defined, but clearly refers to a person who owes an obligation to the applicant under a claim or, where an applicant has standing to commence proceedings on the basis of subsection 6(2) before an obligation has arisen, to the person who potentially owes an obligation to the applicant in the underlying litigation.

Clause 7(1)(a) defines conditions under which the ability of unsecured creditors to recover their claims is inherently defeated or impeded by a transaction. A person who is insolvent is by definition unable to or has ceased to satisfy creditors' claims (see s. 1(1) "insolvent"). Since a transaction directly or indirectly diminishes the asset base against which creditors may enforce their claims, a transaction under which an insolvent debtor receives no compensating value or value worth less than the value conferred on the transferee will adversely affect creditors. The same result follows if the debtor is rendered insolvent by the transaction or becomes insolvent shortly thereafter while creditors remain unsatisfied.

The grounds for relief prescribed by both clauses 7(1)(a) and (b) refer to the amount of "consideration" received by the debtor. This usage should not be read too narrowly. It does not assume that the transaction in question involves a contractual relationship or voluntary exchange between the debtor and the transferee, but refers more generally to receipt by the debtor of something that constitutes value in law. For example, if a debtor pays a debt secured by a security interest in his or her property, the release of the security interest constitutes consideration received by the debtor in the relevant sense. The value of the consideration in such a case is commensurate with the benefit conferred on the transferee creditor through payment. Although the transaction involves satisfaction of a claim, it is by definition not a creditor transaction (see s. 1(1) "creditor transaction" clause (b)) so it cannot be challenged under Part III. While the transaction may be the subject of an application under Part II, relief could not be granted under clauses 7(1)(a) or (b) because the lack-of-consideration requirement is not satisfied.

The requirement that the debtor received no consideration or consideration "conspicuously less than" the value conferred on the transferee means relief is available only if the transferee is in a position to recognize that he or she is dealing with the debtor on such unreasonable terms that the transaction may have adverse ramifications. The concept is not unique. Under the reviewable transaction rules of the federal *Bankruptcy and Insolvency Act*, a transfer at undervalue "means a disposition of property or provision of services for which no consideration is received by the debtor or for which the consideration received by the debtor is *conspicuously less than* the fair market value of the consideration given by the debtor (emphasis added)." Authorities that address the meaning of the *BIA* definition may be relevant to the corresponding terms of this Act.

Clauses 7(1)(b) and (c) require proof that the debtor's primary intention in relation to the transaction was to hinder or defeat the right of a creditor or creditors to recover an existing claim, or a claim that was reasonably foreseeable at that time. If the debtor is insolvent or verging on insolvency, that fact may be evidence of an intention to avoid creditors' claims (see s. 7(3)(a)). However insolvency is not a condition of relief under these clauses; an order may be granted against a person who has accepted a benefit from a perfectly solvent debtor if the debtor's intention is in fact realized as provided by subclause (b)(i) or (c)(ii), as the case may be.

The phrase "primary intention" recognizes that a transaction may be intended both to defeat creditors and to achieve some other purpose, such as to assist a friend or family member or to realize a tax advantage. The question of whether the "primary" intention was to defeat or hinder creditors should be approached objectively, taking into account the actual effect of the transaction and factual indicia of intention, including those

listed in subsection 7(3). If the debtor entered into a transaction that would obviously defeat creditors' claims, the attainment of that outcome may be regarded as the debtor's primary intention in spite of the presence of other motives. However, there are cases in which an intended result other than to defeat creditors should be recognized, even though a transaction may have that effect. This is particularly so in relation to a transaction between spouses or former spouses prompted by the collapse of the spousal relationship and effectuated by a genuine separation agreement or a court order (see comment on s. 8(2)).

Relief is available under clauses 7(1)(b) or (c) only if creditors' ability to recover their claims against the debtor was materially hindered as a result of the transaction. This requirement will rarely be met if the debtor is solvent, since a solvent debtor ordinarily has exigible assets that are worth enough to satisfy creditors' claims (see s. 1(1) "insolvent" clause (c)). Nevertheless, creditors may be materially hindered in the relevant sense if a transaction converts assets that can be reached under judgment enforcement measures into assets that are removed from the jurisdiction or against which enforcement is otherwise prohibitively difficult. The question is whether the result of the transaction was to make it significantly difficult if not entirely impossible for creditors to enforce their claims. The grounds for relief defined by clause 7(1)(c) will rarely be established, since the applicant must prove both that the debtor intended to hinder or defeat creditors and that the transferee knew of and intended to assist in achieving that objective. Again, the intention of both parties must be determined objectively. Subsection 7(3) provides a non-exhaustive list of factors that may be relevant. If the intention requirements are met and the transaction in fact materially hinders the ability of creditors to recover their claims, an order for relief may be made regardless of whether the transferee gave full consideration for the benefit received under the transaction.

The Act does not allow a transaction to be challenged simply because it results in the exchange of non-exempt for exempt assets. Such a transaction will ordinarily not fall within clauses 7(1)(a) or (b) because the exempt asset acquired will constitute full consideration received by the debtor in exchange for the property transferred to the transferee. For example, the investment of exigible funds in an exempt RRSP involves an exchange of equivalent value between the investing debtor and the financial institution holding the investment; the obligations owed to the debtor by the institution after the funds are received are worth roughly the amount invested. Relief may be available under clause 7(1)(c) in relation to the acquisition of exempt property if the transferee participated in the exchange with the intention of assisting the debtor's intention to defeat creditors. The fact that the transferee gave full consideration is not an obstacle to relief if the requisite intention is proven.

(2) For the purposes of subsection (1), if the transaction involves a corporation repurchasing or redeeming shares issued by the corporation, neither receipt of the shares by the corporation nor their surrender by the holder is to be regarded as consideration received by the corporation under the transaction.

Comment: Subsection 7(2) deals with the special case of a transaction under which a corporation pays a shareholder to repurchase or redeems its own shares (see s. 1(1) "transaction" clause (h)). The return or surrender of the shares adds nothing to the asset base of the corporation and should not be

regarded as consideration for the payment received by the shareholder transferee. An order for relief is available against a benefitted shareholder if the circumstances fall within any of the grounds of relief established by subsection 7(1). Section 9 provides for a supplementary order for relief against a director of the corporation. Subsections 9(5) and 9(7) are designed to ensure that a shareholder is not liable to disgorge a payment received from the corporation both under this Act and corporations legislation (see comment on s. 9).

(3) The court may consider the following factors, among others, in determining the intention of the debtor or the transferee:

(a) in the case of the debtor, whether the debtor was insolvent at the date of the transaction or became insolvent as a result of the transaction;

(b) in the case of the transferee, whether the transferee knew that the debtor was insolvent at the date of the transaction or would likely become insolvent as a result of the transaction;

(c) whether the transaction occurred at a time when the debtor or the transferee, as the case may be, knew of the existence of a claim against the debtor or had reasonable grounds to anticipate that a claim would arise in the foreseeable future;

(d) if the transaction was effected by a court order,

(i) in the case of the debtor, whether the debtor failed to disclose to the court in the proceedings under which that court order was made

(A) an existing or reasonably foreseeable claim that may be prejudiced by the order, or

(B) the extent of an existing or reasonably foreseeable claim, or

(ii) in the case of the transferee, whether the transferee failed to disclose to the court in the proceedings under which that court order was made

(A) an existing or reasonably foreseeable claim that may be prejudiced by the order and that was known to the transferee, or

(B) the extent of an existing or reasonably foreseeable claim that was known to the transferee;

(e) whether the value of the consideration received by the debtor was less than the value of the benefit conferred on the transferee;

(f) whether the parties to the transaction were related or closely affiliated;

(g) whether the debtor retained the possession, use or benefit of property or value transferred under the transaction;

(h) whether the transaction was entered into in haste;

(i) whether the debtor or the transferee attempted to keep the transaction or circumstances material to the availability of relief under this Act hidden from creditors or others;

(j) whether the transaction was not documented in the manner that would ordinarily be expected in relation to a transaction of that kind.

Comment: Subsection 7(3) lists factors that may be taken into account by the court in determining whether a debtor or transferee entered into a transaction with the intention indicated in clause 7(1)(b) or (c). Many of the factors listed reflect the "badges of fraud" often referred to in pre-reform cases as evidence that a debtor intended to hinder, defeat, delay or prejudice creditors. The existence of one or more of the circumstances identified does not raise a presumption of intention but rather weighs in the balance of evidence before the court. However, evidence of a listed factor may be accepted by the court as proof of the intention required if no credible countervailing evidence is presented. Clause 7(3)(d) may be of particular significance in relation to a spousal transaction effected by a court order, which may only be challenged under clause 7(1)(c) (see comment on s. 8(1)).

Relief in certain cases

8(1) In this section, "contingent obligation" means an obligation to pay money, transfer property or otherwise give value, the performance of which is contingent on an event that may or may not occur, and includes an obligation under a guarantee or an agreement to indemnify against loss occasioned by the default or non-performance of another person.

(2) An order for relief may be made in relation to the following transactions only if the grounds for relief mentioned in clause 7(1)(c) are established:

(a) a spousal transaction;

(b) a transaction involving the refusal by a debtor to act under a power of appointment to confer an interest in property on the debtor or the disclaimer of an interest in property before the interest has vested; or

(c) a transaction involving the assumption of a contingent obligation by the debtor.

Comment: Subsection 7(1) establishes three sets of conditions that warrant an order for relief in relation to a transaction entered into by a debtor. Section 8 limits the application of subsection 7(1). Relief is available only under the provisions identified in relation to a transaction described in subsection 8(2) or 8(3). Subsection 8(3) is broader in scope than 8(2). If a transaction falls within both, the more restrictive rules of subsection 8(2) apply.

Subsection 8(2) restricts the grounds of relief to those defined by clause 7(1)(c) if a transaction is one of the three types indicated. The applicant must prove both that the debtor's primary intention was to defeat or hinder a creditor or creditors and that the benefitting transferee knew of and intended to assist in the achievement of that intention.

Clause (a): Clause 8(2)(a) applies to a spousal transaction, defined in subsection 1(1). A transaction between family members that is not a spousal transaction may be challenged under any of the provisions of subsection 7(1). However, the transferee may be sheltered in appropriate cases by the court's discretion under subsection 18(4) to deny or adjust an order where a transferee has acted in reasonable reliance on the finality of the transaction (see comment on s. 18(4)).

The restriction of relief to circumstances falling within clause 7(1)(c) in relation to a spousal transaction is designed to ensure that a bona fide settlement of affairs between separating spouses is not readily disrupted. The essential question for the court is whether the transaction was intended by the parties as a creditor avoidance device or a legitimate settlement of spousal and family affairs necessitated by the breakdown of their relationship. Although the grounds for relief under clause 7(1)(c) are difficult to establish, the question of intention may be determined objectively on the basis of the factors indicated in subsection 7(3) and any other relevant circumstances. Clause 7(3)(d) is of particular significance when a transaction is effected by a court order. Parties to spousal litigation are routinely expected to disclose debts as well as assets and the failure to do so will be a strong indication that the order was obtained primarily to defeat creditors. Clause 7(3)(e) may be relevant but should be applied with discretion in relation to spousal transactions. An obvious lack of consideration from a benefitted spouse may be an indication of intention to avoid creditors but the release of a spousal claim is often prompted by emotional and pragmatic considerations that are impossible to value properly in monetary terms.

Section 14 and subsection 10(2) address the fact that a spousal transaction may be regarded as a creditor transaction to the extent that the benefit conferred represents satisfaction of an obligation owed to the transferee spouse. Section 14 states that the creditor transaction rules in Part III do not apply to a spousal transaction and subsection 10(2) confirms that relief is available under Part II, regardless of whether the transaction is a creditor transaction in whole or in part.

Clause (b): Clause 8(2)(b) applies if a debtor refuses property to which he or she is legally entitled under a bequest or on some other basis, or declines to exercise a power of appointment that could have been exercised in his or her own favour (see s. 1(1) "transaction" clauses (i) and (j)). The transaction in such a case is between the debtor and the person or persons who benefit as a result of the debtor's disclaimer or refusal (see s. 1(1) "transferee"). Relief is available only if the debtor intended to keep the property that he or she would have received out of the reach of his or her creditors and the benefitting party (transferee) knew of the debtor's intention and assisted in its fulfilment by accepted the property.

Clause (c): Clause 8(2)(c) applies when a debtor assumes a contingent obligation as defined by subsection 8(1). A contingent obligation entails a present legal obligation to perform in the future if a condition that may or may not occur does occur. The most common cases are those in which a debtor guarantees payment of a debt owed by another person or agrees to indemnify against loss occasioned by another person's default. The person for whom the debtor acts as surety typically benefits by the procurement of a new loan or credit or through forbearance by an existing creditor. The debtor's assumption of the obligation to make good the debt or indemnify against loss may therefore be regarded as a transaction between the debtor and the principal debtor or the person whose non-performance is the basis of the debtor's liability (see s. 1(1) "transaction" clause (m) and "transferee"). Relief is available in relation to such a transaction if it was intended by the debtor to hinder or avoid his or her creditors and the transferee knowingly participated in the achievement of that result.

Example
Debtor and Associate are related companies. Debtor guarantees Associate's debt to Bank. Associate defaults in paying Bank and Debtor pays on the guarantee. The result is an indirect transfer of the amount paid from Debtor to Associate and a corresponding reduction of the assets available to Debtor's creditors. If Debtor and Associate acted under a joint plan to avoid Debtor's creditor's through the guarantee arrangement, an order for relief may be made against Associate.

(3) If a transaction, other than a spousal transaction, is effected by a court order or by operation of law, an order for relief may be made only if the grounds for relief mentioned in clause 7(1)(b) or (c) are established.

Comment: The definition of "transaction" recognizes that a debtor may be obliged to confer a benefit on a transferee under a court order or due to the operation of a rule of law. This ensures that a debtor cannot avoid the Act through the stratagem of obtaining a court order to effect a transfer of value that would otherwise be caught, or by arranging his or her affairs in a way that will activate a rule of law to achieve that result. Subsection 8(3) provides that a transaction effected by those means may only be challenged if the conditions specified in clause 7(1)(b) or (c) are established. Both require proof that the debtor participated in procurement of the order or in arranging events to activate the rule of law with the primary intention of hindering or defeating the rights of a creditor or creditors generally. Clause 8(1)(a) applies to a spousal transaction effected by an order of the court.

(4) If a transaction is effected by a court order, an order for relief may be made by any court having jurisdiction to grant relief under this Act, whether or not that court is the court that made the order effecting the transaction.

Transactions involving corporate payments

9(1) This section applies to a transaction that consists of the purchase or redemption of its shares by a debtor corporation or the declaration of dividends by a debtor corporation.

(2) If an order for relief is made against a shareholder as transferee in a transaction, the court may make an order for relief against a director or directors of the corporation, jointly and severally, [*for jurisdictions based on the civil law* - solidarily], to take effect if and to the extent that the order against the shareholder is not satisfied within 6 months after the date that the order is made.

(3) An order for relief must not be made under this section against

(a) a director who is not liable in relation to the actions constituting the transaction under any applicable Act or other law governing the corporation that provides for a remedy against a director in relation to a resolution or action authorizing the purchase or redemption of shares or the declaration of a dividend; or

(b) a director who had reasonable grounds to believe that the circumstances of the transaction were such that the transaction did not give rise to a remedy under the Act or law mentioned in clause (a).

(4) In determining whether a director had reasonable grounds within the meaning of subsection (3), the court must consider whether the director in

good faith relied on, and whether a reasonable person in the director's position could be expected to rely on,

(a) financial statements of the corporation represented to the director by an officer of the corporation or in a written report of the auditor of the corporation to reflect fairly the financial condition of the corporation; or

(b) a report of a lawyer, accountant, engineer, appraiser or other person whose position or profession lends credibility to his or her statement.

(5) An order for relief must not be granted against a shareholder who, in proceedings taken under the *Canada Business Corporations Act* or the [*insert name of provincial or territorial business corporations statute*] by the corporation or another person, has been ordered to restore to the corporation or to a director of the corporation any amount paid or the value of property distributed under the transaction.

(6) An order for relief must not be granted against a director who, in proceedings taken under the *Canada Business Corporations Act* or the [*insert name of provincial or territorial business corporations statute*] by the corporation or another person, has been ordered

(a) to restore to the corporation any amount paid or the value of property distributed under the transaction; or

(b) to make a payment to satisfy a right of contribution held by another director who has been ordered to restore to the corporation any amount paid or the value of property distributed under the transaction.

(7) If an order for relief is made against a shareholder or a director in relation to a transaction,

(a) the order is not enforceable against that person if the person is subsequently ordered in proceedings under the *Canada Business Corporations Act* or under the [*insert name of provincial or territorial business corporations statute*]

(i) to restore to the corporation an amount paid or the value of property distributed under the transaction, or

(ii) to satisfy an order for contribution; and

(b) the court may suspend enforcement of the order for relief until proceedings against that person under the *Canada Business Corporations Act* or under the [*insert name of provincial or territorial business corporations statute*] are concluded.

Comment: The payment of a dividend by a corporation or the voluntary purchase or redemption of its shares is a "transaction" between the corporation and the benefitting shareholder (see s. 1(1) "transaction" clause (h)). An order for relief may be made against the shareholder under subsection 7(1) if grounds for relief are established (and see comment on s. 7(2)). However, subsections 9(5) and 9(7) may be relevant (see below). The former restricts the availability of relief and the latter restricts enforcement of an order already obtained.

When relief is granted against a shareholder in relation to a transaction described in subsection 9(1), subsection 9(2) authorizes the court to make a supplementary order against a director of the corporation who is responsible for authorizing the payment. A director may also be liable to the corporation in relation to the declaration of a dividend or the repurchase

or redemption of shares under a federal or provincial corporations statute if the corporation is insolvent at the time of the payment or is likely to become insolvent as a result. Creditors of the corporation are generally not entitled to relief under such legislation. Section 9 offers relief to creditors in circumstances that approximate those under which a director might be liable to the corporation. However, qualifications are imposed on the right to relief.

Subsection 9(3) provides in effect that if a director is not liable under an applicable federal or provincial corporations statute in relation to the action in question, or if the director had reasonable grounds to believe that he or was not liable under that law, he or she is similarly not liable under this Act. Directors are not obliged to consider whether a course of action that is valid under the law governing the corporation may give rise to liability under reviewable transactions law.

Subsection 9(6) deals with the possibility that an application for relief may be made under this Act against a director who is liable under a corporations statute for the same course of conduct. The objective is to avoid imposing liability twice for the same action. If an order has been made against a director under the corporations statute, relief may not be granted under this Act. Subsection 9(5) provides similar protection to a shareholder, who may be obliged under corporations legislation to return a dividend payment made by an insolvent corporation or a sum paid by an insolvent corporation for the repurchase or redemption of its shares.

Subsection 9(7) applies when an order for relief has been made against a director or shareholder under this Act but not satisfied or enforced before proceedings are taken under the corporations statute. The court may suspend an order for relief under this Act until proceedings under the corporations law are concluded and an order made under this Act ceases to be enforceable if relief is granted under the corporations statute. The Act does not provide for a case in which an order for relief under this Act has been made and satisfied or enforced before proceedings are taken under the corporations statute. Relief under corporations law could be precluded by amendment of the corporations legislation to that effect.

The provisions of Part IV that apply generally to relief under Part II apply to an order made against a shareholder. Subsection 22(2) provides a separate rule for relief against a corporate director.

Orders for relief respecting creditor transactions

10(1) Subject to subsection (2), if a transaction is a creditor transaction, an order for relief may be made under this Part only to the extent that the value of the benefit conferred on the creditor exceeds the claim satisfied or secured by the creditor transaction.

(2) This Part applies to a spousal transaction, whether or not the spousal transaction is a creditor transaction in whole or in part.

Comment: An order for relief may be granted only under Part III in relation to a transaction that falls within the definition of "creditor transaction". However, if the benefit conferred on a creditor is worth more than the debt owed, any surplus value received is treated as a separate transaction that may be challenged under Part II.

Example

Debtor owes Creditor $50,000. Debtor transfers an asset worth $75,000 to Creditor in satisfaction of the debt. The transaction is a creditor payment to the extent of $50,000 and may only be

challenged under Part III. The $25,000 benefit gratuitously conferred on Creditor may be challenged as a transaction under Part II and an order for relief made against Creditor to the extent of that amount if grounds for relief are established.

Subsection 10(1) implicitly allows the court to determine the actual value of a claim owed to a creditor for purposes of determining the availability of relief under Part II. In the example given, Debtor and Creditor could not avoid Part II by agreeing to an exorbitant rate of interest on the debt or by inflating its amount to $75,000 through other untenable accounting or payment practices. The court may find on the evidence that the actual amount owed to a creditor is less than the amount declared by the parties.

Subsection 10(2) provides an exception to subsection 10(1) in the case of a transaction falling within the definition of "spousal transaction". A payment or transfer of property made to achieve a division of property or provide financial support may be regarded as a creditor transaction to the extent that it involves the satisfaction of a claim held by the benefitting spouse. However, section 14 provides that an order for relief may not be made under Part III in relation to a spousal transaction. The result is that a spousal transaction may be challenged under Part II but not under Part III.

Persons against whom relief may be granted under this Part

11(1) If grounds for relief mentioned in section 7 are established, the court may make an order for relief against either or both of the following:

(a) a transferee who received a benefit from the debtor under the transaction;

(b) subject to subsection (2), a person who has received all or part of the benefit conferred under the transaction from a person described in clause (a) or a subsequent transferee.

(2) An order for relief must not be made against a person mentioned in clause (1)(b) if the person gave consideration that, in the opinion of the court, is worth not conspicuously less than the value of the benefit received and

(a) if the grounds for relief fall within clause 7(1)(a), the person did not know that the benefit derived from a transaction that occurred in the circumstances described in that clause; or

(b) if the grounds for relief fall within clause 7(1)(b) or (c), the person did not know that the benefit derived from a transaction in which the debtor's primary intention was to hinder or defeat the enforcement of the rights of a creditor or creditors.

(3) If grounds for relief mentioned in section 9 are established, the court may make an order for relief against a director of a corporation.

Comment: Clause 11(1)(a) provides for an order for relief against a transferee, who is by definition a person who benefits under a transaction (see s. 1(1) "transferee"). A transferee usually receives property or value in some other form directly from a debtor. In some cases, a transferee is a person who benefits indirectly as the result of a debtor's dealing with someone else (see comments on s. 1(1) "transaction" and s. 8(2)(c) for examples). However the transaction is effected, an order for relief may be made against the transferee and implicitly not against the debtor. The

objective is to restore the value of the benefit obtained by the transferee to the debtor's creditors. Part IV determines the terms of the order.

Clause 11(1)(b) deals with a case in which the debtor confers a benefit on a transferee who then transfers the benefit to a second person. The second transferee may transfer the benefit to a third, and so on. An order may be made against a person who has obtained the benefit originally conferred on a transferee as the result of a secondary or subsequent transfer. Creditors' rights could be seriously compromised if they could only follow value alienated by a debtor into the hands of the first recipient. Relief may be granted against a secondary or subsequent transferee only if the circumstances of the original transaction constituted grounds for relief under Part II and only subject to the limitations imposed by subsection 11(2). An order may not be made against those who have given consideration worth not conspicuously less than the value of the benefits they themselves have received and who do not know that the benefit derived from a transaction that involved circumstances giving rise to a right to relief under subsection 7(1). The rules in subsection 1(4) apply in determining whether a person has knowledge of the relevant facts.

> **Example**
> Debtor, who is insolvent, transfers property to Transferee for no consideration. Grounds for relief against Transferee under clause 7(1)(a) are established. Transferee gives the property to Transferee 2, who sells it to Transferee 3 for a price approximating its market value.

In the example, clause 11(1)(a) allows for an order against Transferee. Clause 11(1)(b) allows for an order against Transferee 2. Subsection 11(2) does not bar relief because Transferee 2 gave no consideration for the benefit received under the transaction, regardless of whether he or she knew of the circumstances of the original transaction. Since Transferee 3 has given consideration worth not conspicuously less than the benefit received, an order for relief is precluded unless he or she knew that the property was originally transferred away by an insolvent debtor for no consideration. A similar approach is taken under the federal *Bankruptcy and Insolvency Act* provisions that apply to a transfer at undervalue or preference, which allow the trustee to recover against a secondary transferee who has not "paid or given in good faith adequate valuable consideration."

PART III
Preferential Creditor Transactions

Introductory comment: The rationale for Part III is explained briefly in the introduction to the Act. Relief under this Part is designed to buttress the creditor sharing rules of provincial and territorial law. In the common law jurisdictions, these rules are generally referred to as creditors' relief law. Under creditors' relief law, funds generated by judgment enforcement measures against a debtor's property must be shared *pro rata* among qualifying unsecured creditors. Those who qualify are generally judgment creditors who have taken a prescribed procedural step to establish their claims, though in some jurisdictions unsecured creditors who hold liquidated claims may be eligible under a certificate filed with the sheriff or distributing authority. Part III offers relief when a creditor transaction infringes on the unrealized sharing rights of unsecured creditors by

allowing one creditor to recover a claim while others cannot. Section 12 identifies the persons who have standing to apply for relief and section 15 identifies those against whom relief may be granted. Section 13 defines the circumstances in which relief is available. Section 14 excludes spousal transactions from this Part. The terms of the order for relief are specified by Part IV. The provisions of Part I also apply to an application under Part III.

Part III applies only to transactions that fall within the section 1(1) definition of "creditor transaction". The adjective "preferential" in the title to this Part signals the rationale for relief; namely, that the transaction has the effect of preferring one creditor over others in terms of their ability to recover debts owed by a common debtor. However, not all transactions that have that result are subject to challenge.

The routine payment of debts is generally not affected by anti-preference law, even though the paid creditor may be advantaged relative to those who remain unpaid. Part III is designed to achieve a substantial degree of consistency between provincial law and federal insolvency law.

Who may apply for order of relief under this Part

12(1) Subject to subsection (2), an application for an order for relief under this Part may be made by a person who holds a claim that existed at the date of the creditor transaction that is the subject of the application for relief.

(2) If a claim is a right to satisfaction of an obligation that is contingent on a future uncertain event, the person who holds the claim may apply for relief only if, at the date of the creditor transaction that is the subject of the application for relief, it was reasonably foreseeable that the event would occur.

Comment: Section 12 provides the rules that determine whether a person has standing under Part III to apply for relief in relation to a creditor transaction. However, the availability of relief may be affected by sections 3, 4 and 5 of Part I, which apply generally to proceedings under the Act.

Subsection 12(1) allows a person who has a "claim" against a debtor at the date of the transaction that is the subject of the application to apply for relief. "Claim" is defined in subsection 1(1) and the date of the transaction is determined under subsection 1(3). Although the definition of "claim" is not limited to an unsecured claim, section 3 precludes an order for relief in favour of a creditor whose claim is fully secured. Subsection 4(2) may bar or limit an order for relief in favour of any claimant in the special case of a creditor transaction involving a transfer of property that is subject to a security interest. Section 5 allows a person who does not have judgment on a claim to apply for relief but requires the applicant to obtain judgment before he or she can benefit under an order against the transferee.

A claim is the right to satisfaction of an obligation owed by a debtor, whether or not the right to satisfaction is absolute or contingent. Subsection 12(2) applies when a person holds a claim that exists at the date of the creditor transaction but the right to satisfaction of the obligation represented by the claim is contingent on an event that may or may not occur. Such a person has standing to seek relief under Part III only if it was reasonably foreseeable at the date of the transaction that the contingent event would occur.

Example

Debtor owes money to Bank. Guarantor guarantees the debt. Debtor, who is insolvent, pays a debt owed to Related Company.

Debtor defaults in paying Bank and Bank seeks recovery from Guarantor.

The payment by Debtor to Related Company is a "creditor transaction". At the time of the transaction, Debtor owed an obligation to indemnify Guarantor against any payment that might be made to Bank under the guarantee but Guarantor's right to satisfaction of that obligation was contingent on a payment being made. Guarantor has standing to apply for relief against Related Company under Part III if it was reasonably foreseeable at the date of the creditor transaction that Guarantor would be required to pay Bank under the guarantee and become entitled to enforce Debtor's obligation to indemnify. The mere possibility that Guarantor may be required to pay Bank is not enough to give Guarantor standing under the rule in subsection 12(2). Subsection 12(2) would not be relevant if Guarantor had already paid under the guarantee at the date of the transaction. In that case, Guarantor would have standing to apply for relief under subsection 12(1) because Debtor's obligation to indemnify would no longer be contingent.

Grounds for relief under this Part - preferential creditor transactions

13(1) Except as otherwise provided in this Act, an order for relief may be made under this Part in relation to a creditor transaction if

(a) the creditor receiving the benefit conferred under the creditor transaction is not dealing at arm's length with the debtor; and

(b) the debtor

(i) is insolvent at the time of the creditor transaction,

(ii) becomes insolvent as a result of the creditor transaction, or

(iii) enters into the creditor transaction in circumstances in which the debtor is demonstrably at risk of insolvency and the debtor becomes insolvent within 6 months after the date of the creditor transaction.

(2) Persons who are related to each other are presumed not to deal with each other at arm's length while so related but the presumption may be rebutted by proof that they are dealing at arm's length.

(3) It is a question of fact whether persons not related to one another were at a particular time dealing with each other at arm's length.

(4) Persons are related to each other when they are related to each other for the purposes of the *Bankruptcy and Insolvency Act* (Canada).

(5) Persons are deemed to be dealing with each other at arm's length with respect to the following:

(a) a margin deposit made by a clearing member with a clearing house; or

(b) a transfer, charge or payment made in connection with financial collateral and in accordance with the provisions of an eligible financial contract.

(6) In this section,

"clearing house" means a body that acts as an intermediary for its clearing members in effecting securities transactions;

"clearing member" means a person engaged in the business of effecting securities transactions who uses a clearing house as intermediary;

"creditor" includes a surety or guarantor for the debt due to the creditor;

"financial collateral" and "eligible financial contract" have the meaning ascribed by the *Bankruptcy and Insolvency Act* (Canada);

"margin deposit" means a payment, deposit or transfer to a clearing house under the rules of the clearing house to assure the performance of the obligations of a clearing member in connection with security transactions, including, without limiting the generality of the foregoing, transactions respecting futures, options or other derivatives or to fulfil any of those obligations.

Comment: Subsection 13(1) defines the grounds for relief under Part III. The application must relate to a "creditor transaction", the person benefiting under the creditor transaction must be a "creditor" who was "not dealing at arm's length with the debtor" and the debtor must be "insolvent" at one of the three points in time identified in clause (b). Each requirement is informed by other provisions of the Act. A "creditor transaction" is defined in subsection 1(1) as a transaction under which a debtor directly or indirectly benefits a creditor by satisfying a claim or providing security for the satisfaction of a claim, subject to certain exceptions. A "creditor" is defined in subsection 1(1) as a person who holds a claim. A guarantor or surety qualifies as a creditor under the general definition because he or she holds a contingent claim against the principal debtor but the definition is explicitly supplemented by section 13(6) for the purposes of Part III to avoid any uncertainty and to clearly parallel the preference rules of the *Bankruptcy and Insolvency Act* (*BIA*). Subsections 13(2) through (5) establish rules that determine whether the creditor and the debtor are dealing with each other at arm's length. "Insolvent" is defined in subsection 1(1).

A solvent debtor is ordinarily in a position to satisfy all his or her financial obligations. Conversely, an insolvent debtor cannot satisfy all such obligations or has ceased to do so - a fact that itself is generally an indication of financial incapacity. When an insolvent debtor pays one creditor leaving others unpaid, the paid creditor is inherently preferred to the extent of the payment because the debtor's financial circumstances are such that the unpaid creditors will not be able to recover fully or at all through enforcement against the debtor's property. The policy basis for legislation that obliges a preferred creditor to disgorge a preferential payment in favour of creditors generally is founded on the legal entitlement of unsecured creditors to recover their claims against property of a common debtor on a *pro rata* basis. Transactions that undermine that entitlement are objectionable. Since *pro rata* sharing rights ordinarily arise only when a debtor becomes bankrupt, anti-preference rules are typically found in bankruptcy legislation. The existence of a *pro rata* sharing scheme under the creditors' relief rules of judgment enforcement law is a uniquely Canadian phenomenon among common law jurisdictions (see Part III introductory comment).

Section 13 reflects a policy choice to define provincial and territorial law in terms that will produce outcomes that are substantially consistent with those produced by the anti-preference rules of the *BIA*. Like the *BIA*, subsection 13(1) offers relief when a payment is made or security for payment given by an insolvent or nearly insolvent debtor to a non-arm's length creditor. Harmonization of outcome is advanced by adopting the *BIA* rules that determine whether persons are at arm's length. Subsections 13(2), 13(3) and 13(5) emulate the *BIA* rules and subsection 13(4) refers the question of whether persons are related to the relatively lengthy *BIA* provisions that determine that issue. Subsection 13(6) adopts the *BIA* definitions that inform the rules in subsection 13(5) as well as the definition applied to the term "creditor" in relation to preferential payments.

The approach taken in subsections 13(2) through (6) means that a transaction that is not at arm's length under the *BIA* is similarly not at arm's length under this Act. Whether a debtor is or is not related to a creditor who benefits under a creditor transaction is an important factor in determining whether the creditor was dealing at arm's length with the debtor for purposes of clause 13(1)(a) but is not conclusive.

Although related persons are presumed under subsection 13(2) not to deal with each other at arm's length, the court may find that a transaction between related persons was in fact an arm's length transaction if the evidence so indicates. Conversely, subsection 13(3) makes it clear that unrelated persons may not be dealing at arm's length with respect to a creditor transaction though they deal at arm's length in other respects. The availability of relief depends on whether the benefitting creditor was dealing at arm's length with the debtor with respect to the creditor transaction in question.

The Act differs from the *BIA* in that it does not offer relief when a payment is made or security given to a creditor who is dealing with the debtor at arm's length in relation to the transaction. The rules that define the circumstances in which arm's length transactions may be avoided under the *BIA* are narrowly drawn and, unlike those that apply to non-arm's length transactions, require proof of intention to prefer. The presumption of intention that arises under the *BIA* from preferential effect may be, and often is, rebutted, with the result that ordinary course transactions and those motivated by normal commercial considerations are generally beyond challenge. The practical difference in outcome between the approach taken to arm's length transactions under the *BIA* and that adopted by the Act is therefore likely to be relatively small.

Non-application of Part to spousal transactions

14 This Part does not apply to a spousal transaction, notwithstanding that the spousal transaction may be a creditor transaction in whole or in part.

Comment: Section 14 applies to a "spousal transaction" as defined in subsection 1(1). The effect of section 14 is explained in the comment on section 10.

Persons against whom relief may be granted under this Part

15 If grounds for relief under this Part are established, the court may make an order for relief against either or both of the following:

(a) the creditor receiving the benefit conferred under the creditor transaction;

(b) a person who has received all or part of the benefit conferred under the creditor transaction

(i) in a transaction with the creditor mentioned in clause (a), if the person was not dealing at arm's length with the creditor, or

(ii) in a transaction with a transferee who received all or part of the benefit from the creditor mentioned in clause (a) or a subsequent transferee, if the parties to each transaction leading to receipt of the benefit by the person against whom relief is claimed were not dealing at arm's length.

Comment: Section 15 is the Part III counterpart of section 11 in Part II. A "creditor transaction" is one in which a debtor directly or indirectly benefits a creditor (see comment on s. 1(1) "creditor transaction"). Clause 15(a) provides for relief against the creditor transferee who initially received the benefit from the debtor. Clause 15(b) allows an order to be made against a person to whom that benefit is transmitted by the creditor transferee, or a person who acquires the benefit under a transaction linked through a chain of transactions with the first. Assume for example that Debtor transfers property to X in circumstances that give rise to relief under section 13. X transfers the property to Y who transfers it to Z. Section 15 allows an order for relief to be made against any of X, Y or Z. However, secondary transferees in the position of Y or Z are liable only if all of the transactions in the chain of dealings were not at arm's length. Y is liable only if he or she was not dealing at arm's length with X. Z is liable only if both the transaction between X and Y and the transaction between Y and Z were not at arm's length.

PART IV
Orders and Remedies

Introductory comment: The remedy offered under the pre-reform law of fraudulent conveyances and fraudulent preferences flowed from the statutory prescription that the transaction in question was void as against creditors. Although the implications of that approach were not entirely clear, it was generally understood that property gained by the transferee was to be made available to satisfy the claims of the transferor's creditors. Part IV of the Act offers a more nuanced form of relief and detailed rules that define the rights of those who are involved in a transaction or may be affected by an order.

The court is directed to craft an order for relief that will achieve a result stated as a general principle. Section 16 applies to relief under Part II and section 17 to relief under Part III. Subsection 18(2) offers a non-exhaustive list of types or forms of order that might be granted by the court alone or in combination to achieve the result prescribed by sections 16 and 17. Subsections 18(4) and 18(6) identify factors that the court should take into account in tailoring the order for relief. Subsection 18(3) ensures that the benefit of an order for relief is shared by all creditors of the debtor who are entitled to participate in the proceeds of judgment enforcement measures under the creditors' relief rules of the judgment enforcement system (see Part III introductory comment and the comment on s. 18(3)). Section 19 deals with the status of a security interest granted under subsections 18(4) or (6) as an element of an order for relief. Section 23 allows

the court to grant injunctive relief before a final order is made and section 24 contains the limitation of actions rules.

The other provisions of Part IV address specific issues that will arise in only a few cases. Section 22 deals with the special case of an order for relief made against the director of a corporation under section 9.

Part II provides for relief in relation to a "transaction", including the subcategory "spousal transaction". Part III provides for relief in relation to a "creditor transaction", which is also a subcategory of "transaction". Since most of the provisions of this Part refer generally to an order for relief or to relief in relation to a "transaction", they apply to relief under both Part II and Part III except as otherwise provided.

Nature of order under Part II

16 In granting relief under Part II, the court shall make any orders that it considers necessary to make available to the person who applies for relief the value conferred on the transferee under the transaction to the extent of that person's claim against the debtor, taking into account the provisions of section 18.

Comment: Section 16 reflects the rationale for relief under Part II. A transaction is objectionable when it has the effect of reducing the amount or value of a debtor's property that is available through the judgment enforcement system to satisfy the claims of unsecured creditors. The transferee who receives property or value that detracts from the debtor's estate has gained at the creditors' expense. If the circumstances are such that grounds for relief are established, the order for relief requires the transferee to disgorge the value obtained under the transaction in favour of the applicant claimant to the extent of his or her claim. Section 18 provides detailed rules regarding the terms through which the objective stated in section 16 may be achieved. Subsection 18(4) makes it clear that, except as provided by section 18(5), the transferee is not obliged to enhance creditors' recovery by relinquishing property or value for which consideration was given. The objective is to restore to creditors the value gained by a transferee and thereby lost to them, but no more.

Example 1

Debtor owns property worth $100,000 before entering into a transaction with Transferee. Debtor sells an asset that has a market value of $40,000 to Transferee for $20,000. The result is to reduce the net value of Debtor's estate by $20,000. Transferee has received a gratuitous benefit to the extent of the $20,000 value received in excess of the amount paid. Creditor, who holds a $30,000 claim against Debtor, applies for relief under Part II. If grounds for relief are established, the order should require Transferee to pay $20,000 to Creditor or to otherwise make property worth $20,000 available to satisfy Creditor's claim. If Creditor's claim against Debtor was only $10,000, the order against Transferee should be limited to that amount.

Example 2

Debtor owns property worth $100,000 before entering into a transaction with Transferee. Debtor provides professional services that have a market value of $40,000 to Transferee for $20,000. Since Debtor could have obtained full value for the services either from Transferee or from another person, the result of the transaction is to reduce the net value of Debtor's estate by

$20,000. As in Example 1, Transferee has received a gratuitous benefit to the extent of the $20,000 value received in excess of the amount paid and if grounds for relief are established, the order should be designed to achieve the same result.

The orders for relief in the two examples given are designed to achieve the same result but their terms may differ. We will assume that the applicant creditor holds a claim worth $20,000 or more so is entitled to recover in that amount. The court could achieve that result in both cases by granting a $20,000 money judgment against Transferee. In Example 1 there are a number of other alternatives. The court could order that the asset be sold and $20,000 of the proceeds paid to Transferee with the balance to the applicant. Alternatively, it could allow the applicant to take judgment enforcement measures against the asset in the hands of Transferee. In the further alternative, the court could (1) order that the asset revest in Debtor where it would be subject to judgment enforcement measures taken by the applicant and (2) grant judgment in the amount of $20,000 against Debtor in favour of Transferee as compensation for the $20,000 paid for the asset. The court will chose the order that is most likely to be effective in satisfying the applicant creditor's claim at the least cost while taking into account the repercussions suffered by the transferee under the available alternatives. If the debtor has creditors other than the applicant, the need to formulate an order in terms that will make property recovered available to those who qualify to participate in a distribution under the creditors' relief rules of judgment enforcement law will be a factor (see s. 18(3)).

Section 16 limits the extent of the order for relief to the amount of the applicant's claim. The applicant is not required to prove the existence or extent of other claims but others may join in the proceedings. Joint proceedings will be to the applicant's advantage if they allow for a greater recovery based on the cumulative value of the applicants' claims, since whatever is recovered will be subject to the creditors' relief rules.

Nature of order under Part III

17(1) In granting relief under Part III, the court shall make any orders that it considers necessary to set aside the creditor transaction, taking into account the provisions of section 18.

Comment: Section 17 reflects the rationale for relief under Part III. When a payment or the provision of security has the effect of allowing the benefitting creditor to recover a claim while others remain unpaid, the remedy offered is designed to set aside or reverse the payment or the provision of security to the extent of the applicant's claim. In effect, the applicant creditor is entitled to recover from the transferee what could have been recovered from the debtor if the creditor transaction had not occurred. Section 18 lists a range of orders that might be granted to set aside the payment and make the value received available to the applicant and indirectly to other creditors entitled to share under creditors' relief law. The fact that consideration was given by the transferee is not taken into account in the framing of the order since the objective of relief is not to restore to creditors generally a gratuitous benefit received by one but to ensure that all creditors obtain an equivalent measure of satisfaction.

Like section 16, section 17 limits the extent of the order for relief to the amount of the applicant's claim. The applicant is not required to prove the existence or extent of other claims but others may join in the proceedings.

Joint proceedings will be to the applicant's advantage if they allow for a greater recovery based on the cumulative value of the applicants' claims, since whatever is recovered will be subject to the creditors' relief rules.

(2) If an order for relief is made under Part III in relation to a creditor transaction that had the effect of discharging an obligation under a guarantee or indemnity or an obligation secured by a guarantee or indemnity, the obligation so discharged is revived to the extent that the payment is set aside, subject to any defences that the person who owes the obligation may otherwise be entitled to assert.

Comment: Subsection 17(2) is relevant when a creditor transaction relates to a debt that is secured by a guarantee or an indemnity agreement. In the case of a guarantee, the guarantor assumes an obligation to pay a debt owed by a principal debtor to the creditor to whom the guarantee is given in the event of the principal debtor's default. An indemnity agreement involves an agreement under which one person agrees to indemnify a second person against loss occasioned by a third person's failure to perform an obligation owed to the second. We will use the case of the guarantee as the point of reference for purposes of explanation.

Subsection 17(2) deals with two potential scenarios. A payment made by a principal debtor to a creditor in satisfaction of a debt guaranteed by a guarantor is a creditor transaction. A payment made by the guarantor to the creditor in satisfaction of the obligation assumed under the guarantee is also a creditor transaction. Either type of transaction might be challenged by the creditors of the paying party if grounds for relief under Part III exist.

When a principal debtor pays a debt that is secured by a guarantee, the result is generally to discharge the guarantor's obligation to the creditor to the extent that the debt is satisfied. Subsection 17(2) ensures that if the payment is set aside on application by a creditor of the principal debtor, the guarantor's obligation under the guarantee is revived. The transferee creditor loses the value of the payment but is restored to the position he or she was in before the payment was made. Similarly, when a guarantor pays a creditor pursuant to an obligation under a guarantee, the result of the payment is to discharge the principal debtor to the extent that the debt is satisfied. Subsection 17(2) ensures that if the payment is set aside on application by creditors of the guarantor, the obligation of the principal debtor is revived. Again, the transferee creditor loses the value of the payment but is restored to the position he or she was in before the payment was made. Revival of an obligation under subsection 17(2) does not affect defences against payment that would nullify the obligation on other grounds.

Forms of orders

18(1) In this section, "proceeds" means

(a) identifiable or traceable property that is derived directly or indirectly from any dealing with

(i) the property that is the subject of the transaction, or

(ii) the proceeds of the property that is the subject of the transaction; and

(b) the right to an insurance payment or any other payment as indemnity or compensation for loss of or damage to

(i) the property that is the subject of the transaction, or

(ii) the proceeds of property that is the subject of the transaction.

Comment: Clauses 18(2)(a), (b) and (c) provide for an order of the court affecting property transferred under a transaction. The property may be revested in the debtor, making it available to the applicant under judgment enforcement measures, made subject to judgment enforcement measures taken by the applicant while still owned by the transferee or simply sold to generate funds that will be distributed in the manner required by the principle established in section 16 or 17, as the case may be. The concept of proceeds becomes relevant when the transferee has disposed of the property received from the debtor. Although it may no longer be possible to make an order against that property, the court may make an order against "proceeds" property derived from it. An order affecting identified property of the transferee may be preferable to a money judgment, which does not confer rights that may be enforced directly against a specific asset but must be enforced against the property of the transferee through the usual judgment enforcement measures if it remains satisfied.

If a transferee who has received property under a transaction sells or trades it for another item or type of property or otherwise deals with it in such a way as to convert it into another form, the new property is proceeds of the original property. For example, if a car received under a transaction is traded by the transferee for a truck, the truck is proceeds of the car. If money received under a transaction is deposited in a bank account, the account is proceeds of the money. Subclause 18(1)(a)(ii) provides for multiple generations of proceeds. If proceeds property derived from the original property is in turn exchanged for other property, the new property is proceeds of the original property as well as proceeds of the proceeds property. Clause 18(1)(b) provides for a case in which the property subject to a transaction or the proceeds of that property is damaged or destroyed. A resulting right to an insurance or similar payment is proceeds of the original property.

The definition of proceeds tracks the central terms of the definition used in the *Personal Property Security Acts* of the common law jurisdictions, though it applies here to land as well as personal property. The authorities interpreting the *PPSA* provisions replicated in section 18(1) may be applied by extension. Those addressing the requirement that property be "identifiable or traceable" are particularly pertinent. As in the *PPSA*, the term "identifiable" refers in this Act to a case in which property is traded for another item or collection of property that can be identified as a direct substitute. In the first example given above, the truck received in trade for the car is identifiable proceeds of the car. The term "traceable" refers to a case in which the original property has been exchanged for or converted into a form of property that is commingled with other property so that it is not possible to identify which part of the resulting pool was derived from the original property. In the second example above, money received from the debtor was deposited in an account. If the account contained funds from other sources, the account is proceeds of the money only to the extent that it is traceable.

The principles that may be applied or developed to trace property under the *PPSA* are not limited to the common law and equitable rules of tracing. The essential question is whether property in another form is connected with the original property in such a close and substantial way that it may properly be regarded as a substitute for the original. The concept of tracing should be understood here as it is under the *PPSA*, taking into account the

policy and function of the Act and informed by but not limited to the conventional non-statutory tracing rules.

(2) In making an order for relief, the court may make an order or orders that may be required to achieve the result indicated in sections 16 and 17, including

(a) an order vesting in the debtor, or in another person, property that is the subject of the transaction or the proceeds of the property;

(b) an order declaring that property that is the subject of the transaction or the proceeds of that property be subject to judgment enforcement measures in the hands of the transferee;

(c) an order directing that property that is the subject of the transaction or the proceeds of the property be sold and the money realized on the sale distributed as the court may direct;

(d) an order requiring the transferee to pay a sum equivalent to the value of property or other benefits received under the transaction;

(e) except in the case of an order made under Part III, an order requiring the transferee to pay a sum in recognition of income earned through the use or exploitation of property or of a licence, quota, right to use or right to payment received under the transaction;

(f) an order directing the release or discharge of any debt incurred, or security or guarantee given, by the debtor under the transaction;

(g) an order reviving any obligation or security released by the debtor under the transaction;

(h) an order setting aside a designation in favour of a beneficiary;

(i) an order declaring that property that would otherwise be exempt as against creditors is subject to judgment enforcement measures;

(j) an order setting aside or varying a court order if the order constitutes a transaction giving rise to the entitlement to relief;

(k) an order appointing a receiver to take possession of and deal with property in the manner directed;

(l) an order granting an injunction against the debtor or another person.

Comment: Section 18 provides guidance regarding the specific terms through which the relief prescribed by sections 16 and 17, respectively, may be achieved. Subsection 18(2) offers a comprehensive but not exhaustive list of types of order that may be made by the court. The order for relief may comprise a combination of the orders listed and may include other terms. Subsections (3), (4) and (6) must also be taken into account to the extent that they are relevant.

In most cases, the order for relief will simply strip the transferee of the benefit received under a transaction in terms that make its value available to the applicant creditor or creditors. Clause 18(2)(e) goes a step further where an order for relief under Part II relates to a transfer of property that has generated income in the hands of the transferee. The order for relief should make both the property or its value and the income produced by the property after the transfer available to the applicant creditor or creditors. Such an order is justified to the extent that the property could have

generated income if it had remained in the hands of the debtor, since the transaction had the effect of depriving creditors of both the property and the income against which they might have enforced their claims had it not occurred. The provision also applies to a transaction involving a license, quota, right to use or right to payment, any of which similarly may generate income in the hands of the transferee but might not be regarded as property under general principles of property law. Subclause 18(4)(a)(ii) directs the court to take into account expenditures made by the transferee to generate that income as well as non-monetary investments, such as labour. The order should deprive the transferee only of the profit obtained.

Clause 18(2)(a) provides that the court may order that property transferred away under a transaction revest in the debtor-transferor, making it subject to judgment enforcement measures taken by the applicant or any judgment creditor. This approach effectively unwinds the transaction but may be less desirable than other approaches contemplated by subsection 18(2) if judgment enforcement measures against the property will be affected by priority competitions associated with security interests held by other creditors. The court should be cognizant of potential priority issues when framing the terms of an order. Those associated with a security interest granted in favour of a transferee under clause 18(4)(b) or 18(6)(b) are discussed in the comment on section 19. The Act does not deal with a different issue that may arise as the unforeseen consequence of a vesting order. The question is whether the existence of a security interest in the property involved, other than one granted under section 18, will limit or preclude judgment enforcement measures against the property. The answer depends on whether a priority rule created by legislation such as the *Personal Property Security Act* or the *Land Titles Act* applies. The following examples illustrate the problem.

Example 1
Debtor transfers an item of personal property to Transferee. After the transfer occurred, Debtor granted a security interest in all present and after-acquired personal property to Secured Creditor, who registered a financing statement in the relevant Personal Property Registry. When the asset revests in Debtor, the security interest attaches and is perfected. The asset may be seized under judgment enforcement measures but only subject to the security interest, which has priority over the rights of judgment creditors.

Example 2
Debtor transfers an asset to Transferee. A judgment, writ or similar judgment enforcement device was registered against Debtor before the asset was transferred. The asset was also subject to a security interest that was perfected but subordinate to the rights associated with the judgment enforcement device under an applicable statutory priority rule (e.g. giving priority to the first to register). Neither the security interest nor the registered judgment enforcement device are cut off or subordinated to the interest of Transferee under an applicable priority rule. Judgment enforcement measures against the asset will not be affected by the security interest *to the extent of the amount outstanding on the judgment that has priority*. Enforcement measures will produce proceeds that may be allocated to additional judgments only if the asset is worth more than enough to satisfy

the claims associated with both the judgment enforcement device that has priority and the security interest.

An order vesting property in the debtor will not create priority problems if the property in question was subject to a security interest that was cut off or subordinated to the interest of the transferee under a priority rule that applied to the transaction. The secured creditor cannot assert rights based on the security interest when the debtor acquires the property under the vesting order (see s. 3(2)(b)).

(3) An order for relief must be made in those terms or subject to those conditions that the court considers necessary to make money payable or the value of property to be transferred under the order available for distribution to the persons qualified under [*insert name of province's or territory's creditors' relief statute*] to share in the proceeds of judgment enforcement measures taken against the debtor.

Comment: Those who apply for relief under the Act are not required to sue on behalf of creditors generally. However, an order for relief should be designed to ensure that the creditors' relief rules of judgment enforcement law that would operate if a judgment were enforced against the property of the debtor operate in similar fashion when relief is granted against a transferee from the debtor. The effect of subsection 18(3) may be explained by a simple example.

Example
Debtor transfers property to Transferee. Transferee gives no consideration and the circumstances constitute grounds for relief under Part II. Applicant Creditor, whose unsecured claim is worth more than the value of the property, seeks an order against Transferee.

If the transaction had not occurred, Applicant Creditor could have enforced a judgment against Debtor through seizure and sale of the property. However, the proceeds of sale would have been distributed to creditors qualified to share under the distribution system of judgment enforcement law, which include the rules generally referred as creditors' relief rules (see the introduction to the Act and Part III introductory comment). The objective of an order for relief is to make available to Debtor's creditors the property lost to Transferee, or its value. The order should produce an outcome similar to that which would follow if judgment enforcement measures were taken against the property in Debtor's hands. This might be achieved by various means.

If the order for relief directs that property revest in the debtor, the creditors' relief rules will be automatically engaged in favour of other qualifying creditors when the applicant creditor enforces a judgment against the property. If the order for relief directs that the property is subject to judgment enforcement measures in the hands of the transferee, it should also direct that the proceeds of enforcement be distributed under the judgment enforcement rules to creditors of the debtor rather than to creditors of the transferee. If the order for relief directs the transferee to pay a sum of money, the result should be the same. The court should direct that the money paid by the transferee be dealt with in the manner required to invoke the creditors' relief rules that would operate in relation to a judgment against the debtor. This might be accomplished by directing payment to the sheriff, clerk of the court or other enforcement official for distribution under the judgment enforcement law rules. The order could

provide that if the transferee fails to pay a money judgment, the proceeds recovered through enforcement measures against property of the transferee should be paid out by the distributing authority to creditors of the debtor rather than creditors of the transferee, as would otherwise be the case. The transferee's creditors should not be enriched by the property received from the debtor at the expense of creditors of the debtor.

(4) In granting relief under Part II,

(a) subject to subsection (5), the court may refuse an order or adjust the terms of an order, or make an order in favour of the transferee for recovery of an identified sum against the debtor, in recognition of the following:

(i) the value given by the transferee,

(ii) expenditures and non-monetary investments made by the transferee that have increased the value of property received by the transferee under the transaction, or that have generated income through the use of property or of a licence, quota, right to use or right to payment conferred by the debtor, to the extent of the expenditures made or the value invested,

(iii) actions taken by the transferee in reasonable reliance on the finality of the transaction under which a benefit was received; and

(b) if the court orders that property received by the transferee under a transaction or the proceeds of the property be vested in the debtor, the court may grant the transferee a security interest in the property that secures

(i) the value given by the transferee under the transaction, to the extent of that value, and

(ii) expenditures and non-monetary investments made by the transferee that have increased the value of the property, to the extent of the expenditures made or the value invested.

Comment: Clause 18(4)(a) directs the court to consider the factors listed in framing an order for relief to ensure that the legitimate interests of transferees who have acquired a benefit from a debtor are not unfairly sacrificed to the interests of the debtor's creditors. Subsection 18(5) provides that these factors may not be taken into account when relief is granted against a transferee who knowingly acted to accommodate a debtor's deliberate plan to defeat or hinder creditors.

The opening flush of clause 18(4)(a) allows the court to refuse an order or adjust the terms of an order. The discretion to deny relief is designed to respond to circumstances falling within subclause (iii), discussed further below. The factors identified in subclauses (i) and (ii) will affect the amount or type of order made against a transferee, but the refusal of an order on the basis of those factors would undermine the right to relief itself. For example, if an application is made under clause 7(1)(a) or (b), the fact that the transferee has given some consideration should be taken into account in determining the extent of recovery allowed against him or her but is not grounds for denial of an order.

Subclause 18(4)(a)(i) responds to the fact that an order for relief under Part II may be made against a transferee who has given some consideration for the benefit received under a transaction. A transferee who has not knowingly facilitated the obstruction of creditors is obliged to relinquish

only that portion of the benefit not matched by the consideration given. The court may frame the order in various ways. A money judgment against the transferee should be based on the value of the benefit received by the transferee minus the consideration given for that benefit. Alternatively, if the court orders that property transferred under a transaction revest in the debtor so as to make it available to creditors under judgment enforcement measures, it should make "an order in favour of the transferee for recovery of an identified sum against the debtor", that sum being the value of consideration given by the transferee. If the court orders that property received under a transaction should be sold or made subject to judgment enforcement measures in the hands of the transferee, it should direct that the transferee be paid a portion of the proceeds of sale or enforcement representing the consideration given. Clause 18(4)(b) is relevant when the order is cast in terms that require the debtor to pay a sum to the transferee.

Example

Assume that a transferee pays a debtor $40,000 for property worth $100,000. The terms of the order should enable the applicant to recover property or money equivalent to $60,000 from the transferee. The court might order:

(1) that the transferee keep the property but pay $60,000;

(2) that the property be sold and the purchase price of $40,000 repaid to the transferee;

(3) that the property be subject to judgment enforcement measures in the hands of the transferee and $40,000 of the proceeds of enforcement be paid to the transferee before a fund is constituted for distribution to the applicant and other creditors of the debtor qualified to participate; or

(4) that

(a) the property revest in the debtor, and

(b) the debtor pay $40,000 to the transferee. The debt owed to the transferee may be secured by a security interest in the property revested in the debtor or in other property.

An order for relief should also allow the transferee to retain or recover any value invested in improvement of the property received from the debtor or in generating income that is stripped from the transferee under the order. Subclause 18(4)(a)(ii) directs the court to draft an order in terms that will allow a transferee to retain that value "to the extent of the expenditures made or the value invested". When an investment increases the value of property received, the relevant value is the amount invested rather than the increase in value. If the investment is in monetary form, the relevant amount is the sum expended by the transferee. If it is in the form of labour or other non-monetary enhancements, the value of the investment must be assessed. An order may recognize the transferee's investments by reducing the amount of a monetary award against the transferee, by allocating proceeds generated from sale of the property to the transferee or by including an order for payment against the debtor in the transferee's favour.

Subclause 18(4)(a)(iii) gives the court discretion to take into account special circumstances that warrant the moderation or denial of an order for relief even though grounds for relief are established. That discretion should be exercised sparingly to ensure that the predictability of outcomes that the

reformed law aims to achieve is not undermined and that extraneous criteria are not imported into the statutory grounds for relief by judicial practice. A case involving the routine conferral of a moderate benefit on a family member might qualify, as where a reasonable living allowance has been spent or services such as childcare assistance or home improvement are provided on a personal basis.

Clause 18(4)(b) applies when the court makes an order in favour of the transferee against the debtor for recovery of consideration paid for property received under a transaction or for recovery of investments that have increased the value of property received. The problem to which the provision is addressed arises only when the property is revested in the debtor, since in other cases the order of the court will protect the transferee's investment by subtraction from a monetary order against him or her or by an order that he or she receive a portion of the proceeds of sale of the property involved. Although section 19 provides rules that determine the priority of a security interest granted under subsections 18(4) or (6), an order vesting property in the debtor might best be avoided if it would produce a priority competition (see examples given in the comment on s. 19). The court might instead elect to grant an order in terms that allow the transferee to recover or retain his or her investments without requiring a payment by the debtor.

(5) The factors mentioned in subsection (4) are not to operate in favour of a transferee who knew that the debtor entered the transaction with the primary intention of hindering or defeating the enforcement of the rights of a creditor or creditors.

(6) In granting relief under Part III

(a) the court may, in recognition of expenditures and non-monetary investments made by the creditor that have increased the value of property received under the creditor transaction,

(i) adjust the terms of an order, or

(ii) make an order in favour of the creditor receiving the benefits conferred under the creditor transaction for recovery of an identified sum against the debtor; and

(b) if the court orders that property received by the creditor under the creditor transaction or its proceeds be vested in the debtor, the court may grant the creditor a security interest in the property securing expenditures and non-monetary investments made by the creditor that have increased the value of the property, to the extent of the expenditures made or the value invested.

Comment: Clause 18(6)(a) operates in the same way as subclause 18(4)(a)(ii). A creditor who has received a transfer of property under a creditor transaction is entitled to retain or recover investments made in the property that have increased its value. There is no counterpart to clause 18(4)(a)(i) because recovery of the consideration given by the transferee creditor is not appropriate in relation to an order for relief against a creditor transaction. Relief is not based on the gratuitous receipt of value from the debtor but on interference with the entitlement of unsecured creditors generally to share in the benefit received. Clause 18(6)(b) parallels subclause 18(4)(b)(ii).

Security interests created under order for relief

19(1) A security interest granted under subclause 18(4)(b)(i) has priority over the rights of creditors of the debtor that exist in relation to the property when the property vests in the debtor or that arise as a result of the vesting, other than rights associated with a perfected security interest that attached to the property before the transaction occurred.

Comment: Section 19 is relevant only when a transaction involves a transfer of property that is revested in the debtor under an order for relief that includes an order for payment to the transferee secured by a security interest granted under clause 18(4)(b) or 18(6)(b). The rules provided determine the priority of such a security interest relative to a security interest granted by the debtor or to another charge or encumbrance through which creditors' rights may be asserted, such as a judgment enforcement charge or writ.

Subsection 19(1) deals with a case in which the security interest granted by the court secures recovery of the consideration paid for the property acquired under a transaction giving rise to relief under Part II. If the property was subject to a perfected security interest before it was transferred to the transferee, that security interest has priority over a security interest granted to the transferee under clause 18(4)(b)(i). Subsection 19(1) preserves the priority of a security interest in property that was not cut off or subordinated by a priority rule that operated in favour of the transferee but does not result in reinstatement of a security interest that was. When a security interest is cut off or subordinated by a priority rule contained in legislation such as the *Personal Property Security Act* or the *Land Titles Act*, the holder of the security interest may not assert a claim to property recovered in proceedings under this Act on the basis of that interest. The secured party is in the position of an unsecured creditor (see s. 3(2)).

A "perfected" security interest is one that is enforceable against third parties and has a priority status relative to competing interests in the collateral. In the common law jurisdictions, the *Personal Property Security Act* provides rules that determine whether a security interest in personal property is perfected. Although the legislation governing the priority of an interest in land generally does describe a security interest as "perfected", the term should be understood in that context in the generic sense described. A mortgagee's interest in land is a perfected security interest if the mortgage is registered and thereby acquires priority over subsequent interests.

Example 1

Debtor transfers a piece of equipment worth $100,000 to Transferee, who pays $50,000 for it. The equipment was subject to a perfected security interest held by Secured Creditor before it was transferred and the security interest was not cut off or subordinated as a result of the transfer. The court orders that the equipment be revested in Debtor so it can be seized under judgment enforcement measures and orders Debtor to pay $50,000 to Transferee, secured by a security interest in the equipment. Subsection 19(1) provides that Transferee's security interest is subordinate to the security interest held by Secured Creditor. The same result would follow if the transaction involved a transfer of land subject to a registered mortgage held by Secured Creditor.

A security interest granted to the transferee under subclause 18(4)(b)(i) has priority over unperfected security interests and over other charges or encumbrances through which creditors' rights may be asserted, provided the competing interest or encumbrance exists when the property revests in the debtor or arises upon revesting.

> **Example 2**
> Debtor transfers a piece of equipment worth $100,000 to Transferee, who pays $50,0000 for it. After the transfer, Debtor enters into a security agreement with Secured Creditor giving Secured Creditor a security interest in all present and after-acquired personal property of Debtor. The court orders that the equipment be revested in Debtor so it can be seized under judgment enforcement measures and orders Debtor to pay $50,000 to Transferee, secured by a security interest in the equipment. Secured Creditor's security interest will attach to the equipment when Debtor acquires rights in it under the revesting order. Subsection 19(1) provides that the security interest held by Transferee has priority over that held by Secured Creditor, regardless of whether Secured Creditor's interest is perfected.

The result in this example would be the same in the case of a priority competition involving a writ or judgment rather than a security interest. A judgment or writ registered against Debtor that attaches to the equipment when it vests in Debtor is subordinate to a security interest granted to the transferee under subclause 18(4)(b)(i).

Subsection 19(1) speaks to the priority of a security interest granted to a transferee relative to other interests in the property that exist at the date of revesting or that arise automatically when the debtor acquires rights under the vesting order (as in Example 2). The transferee's interest need not be registered or perfected in order to have priority over such interests. However, the rule does not otherwise supplant the priority rules of other legislation that require registration or perfection of a security interest (or some other step) as a condition of priority. The transferee's security interest must be perfected or registered to have priority under such external rules over an interest that arises after the property revests in the debtor. Subsection 19(3) allows the security interest to be registered under the *PPSA* or Land Titles legislation and subsection 19(4) determines the priority status of a security interest so registered.

(2) A security interest granted under subclause 18(4)(b)(ii) or clause 18(6)(b) has priority over the rights of all creditors of the debtor that exist in relation to the property when the property vests in the debtor or that arise as a result of the vesting, including the rights of secured creditors.

Comment: Subsection 19(2) applies to relief under either Part II or Part III, where the court makes an order under subclause 18(4)(b)(ii) or 18(6)(b) granting the transferee a security interest to secure recovery of an investment that has increased the value of property acquired under the transaction. Such a security interest has priority over the rights of all creditors in relation to property revested in the debtor, including a creditor who held a perfected security interest before the transaction occurred. The increased value produced by the transferee's investment is treated as property of the transferee, which he or she is permitted to retain. A prior secured creditor would realize a windfall at the transferee's expense if a pre-existing security interest were given priority over the transferee's interest.

As noted in the comment on subsection 19(1), the transferee's security interest need not be perfected or registered to have priority over interests in the property that exist when the property vests in the debtor or that arise as a result of the vesting, but perfection or registration may be required to establish priority over interests that arise thereafter. Subsections 19(3) and (4) allow the transferee to establish a priority position in relation to subsequent interests.

(3) A security interest in property granted under subsection 18(4) or (6) may be registered

(a) in the Personal Property Registry if the property is personal property, or

(b) in the Land Titles registry if the property is land.

[*Alternative provisions to similar effect will be required in relation to land in jurisdictions that do not use a land titles system.*]

(4) Subject to subsections (1) and (2), a security interest granted under subsection 18(4) or (6)

(a) that is registered in the Personal Property Registry under clause (3)(a) has the status of a security interest perfected by registration under the *Personal Property Security Act*, or

(b) that is registered in the Land Titles registry under clause (3)(b) has the status of an interest in land registered under the *Land Titles Act*

[*or alternative language required in some jurisdictions as noted in relation to subsection (3)*].

Comment: Registration of the transferee's security interest in the Personal Property Registry or the Land Titles registry gives it a priority status in relation to interests in the property other than those that fall within subsections 19(1) and (2). A security interest that is not registered may be subordinated to interests in the property that arise after it revests in the debtor. In jurisdictions in which priority is not based on a registry system, these provisions must be adapted to achieve the same result.

Example
Debtor transfers a piece of equipment worth $100,000 to Transferee, who pays $50,0000 for it. The court orders that the equipment be revested in Debtor so it can be seized under judgment enforcement measures and orders Debtor to pay $50,000 to Transferee, secured by a security interest in the equipment. After the equipment revests in Debtor and before it is sold under judgment enforcement measures taken by the applicant or another judgment creditor, Debtor borrows money from Bank and gives Bank a security interest in the equipment to secure repayment. Bank perfects its interest by registration under the *PPSA*.

Transferee's security interest will have the status of a security interest perfected by registration under the *PPSA* if is registered in the Personal Property Registry. As between the security interests held by Bank and Transferee, the first to register will have priority under the relevant *PPSA* priority rule. Transferee's security interest will also have priority over the trustee in bankruptcy in the event that Debtor becomes bankrupt after the interest is registered.

If the property involved is land, registration in the Land Titles registry gives the transferee's security interest the priority status generally associated with a registered interest in land.

Although the security interest held by a transferee may be subordinated to subsequent interests if it is not registered, that will rarely occur in practice. In most cases, the property in question will be sold under judgment enforcement measures before a subsequent interest arises.

Application of orders for relief to exempt property

20 If an order for relief is granted in relation to a transaction involving exempt property and the debtor continues to use the property in the manner that attracted the exemption, the court

(a) may suspend enforcement of the order for relief until the time that the debtor ceases to use the property in that manner; and

(b) if the enforcement of an order for relief is suspended under clause (a), may order that a [*writ or judgment - depending on the terminology used in provincial judgment enforcement legislation*] be registered against the transferee or the property of the transferee.

Comment: An order for relief may be made in relation to a transaction involving a transfer of property that is exempt from seizure under judgment enforcement measures (see comment on s. 1(1) "transaction"). A debtor who voluntarily disposes of property is presumed not to require it for a purpose attracting an exemption so the fact that the property was exempt before the transaction occurred does not preclude the subsequent enforcement of creditors' claims against it. However, that presumption may not be valid when a debtor transfers away the ownership of property but continues to use it thereafter as he or she did before. For example, a debtor may transfer the title to a house that is exempt as a homestead or personal residence to his or her wife or child but continue to live in it after the transfer. Some courts have dealt with cases of this kind under pre-reform law by directing that a writ be registered against title to the house but suspending enforcement of the writ until the house ceases to be the judgment debtor's residence. Section 20 applies a similar approach to transactions involving exempt property generally.

In most cases, exemptions are based on the use of personal property or land for a purpose that is regarded by the legislature as essential to a basic standard of living. Section 20 applies only when a debtor continues to "use" the property in the relevant fashion. It does not apply if a transaction involves a dealing with an exempt investment such as a registered retirement savings plan, since the debtor does not "use" that type of property after it is transferred to another person.

Section 20 is permissive. A court is not obliged to make an order of the kind indicated though it may do so if the debtor would otherwise be cast out of his or her home, lose the use of his or her only motor vehicle or be seriously affected in some other manner.

Application of Part to subsequent transferees and creditors

21 This Part applies, with any necessary modification, to an order for relief made against a person mentioned in clause 11(1)(b) or 15(b).

Comment: An order for relief will ordinarily be sought against a transferee who has benefitted under a transaction with a debtor and Part IV is addressed primarily to that case. However, clauses 11(1)(b) and 15(b) also

provide for relief against a person who has received the benefit obtained by the first transferee through subsequent transactions. Section 21 makes it clear that the provisions of Part IV apply with such modification as may be required when an order is made against a secondary or subsequent transferee.

Order for relief in relation to corporate payments

22(1) If an application for relief is made in relation to a transaction mentioned in subsection 9(1), subsections 9(2) to (7) must be taken into account in the making or refusal of an order for relief.

(2) If an order for relief is made against a director under section 9, the order must require the director to pay a sum of money equivalent to the amount paid by the corporation under the transaction, and the provisions of this Part, other than subsection 18(3) and sections 23 and 24, do not apply.

Comment: Section 9 contains special rules that apply to an application for relief with respect to a transaction involving the purchase or redemption of its own shares by a corporation or the declaration of dividends by a corporation. Relief may be granted against the shareholder who benefits under the transaction and against a director who has authorized it. Subsection 22(1) flags the provisions of section 9 that may affect the availability of relief in relation to a transaction of that kind.

For the most part, an application for relief against a shareholder is subject to the provisions of the Act that apply to transactions generally. The provisions of Part IV governing an order for relief under Part II apply, subject to the limitations imposed by subsections 9(5) and (7).

Applications for relief against a corporate director are treated differently. The grounds for relief are defined by section 9 and subsection 22(2) provides a special rule governing the terms of an order for relief. In addition, the court must be cognizant of the limitations on relief imposed by subsections 9(2), (3), (4), (6) and (7).

Injunctions

23(1) Whether or not an application for an order for relief has been made, the court may grant an injunction to a person who is, or who may become, entitled to apply for an order for relief under this Act if the court is satisfied that there is a reasonable likelihood that a transaction giving rise to a right to relief has occurred or is about to occur.

(2) In granting an injunction, the court may make any orders against the debtor or another person that the court considers necessary to

(a) preserve the benefit of any final order for relief that may be granted;

(b) allow an appropriate order for relief to be made; or

(c) prevent a transaction from occurring.

(3) Any interested person may apply to the court to vary or terminate an order made under this section.

Comment: Clause 18(2)(l) provides for injunctive relief as part of a final order. Section 23 gives the court jurisdiction to grant an injunction before a final order is granted, whether or not an application for relief has been commenced. An injunction may be required to prevent a transaction that would give rise to relief under the Act from occurring or, if such a transaction has already occurred, to prevent further action on the part of

the debtor or another person that would prejudice the ability of a creditor challenging the transaction to obtain an effective remedy. The principles that govern the granting of injunctions generally will apply to an application for injunctive relief under the Act.

Limitation of actions

24(1) Subject to subsections (2) and (3), no application for an order for relief is to be commenced more than 1 year after the date of a transaction.

Comment: The date of a transaction is determined under subsection 1(3).

(2) If the transferee conceals or assists in the concealment of the transaction that is the subject of the application for relief or of facts material to the grounds for relief, the 1-year period mentioned in subsection (1) commences at the time that the person making the application knew of the transaction or the material facts, but no application for relief is to be commenced more than 5 years from the date of the transaction.

Comment: An order for relief impacts the transferee, not the debtor. Therefore concealment of facts by the debtor does not affect the limitation period if the transferee is not involved.

(3) If the debtor becomes bankrupt before the end of the 1-year period mentioned in subsection (1), the debtor's trustee in bankruptcy may bring an application for an order for relief if the transaction that is the subject of the application for relief occurred during the period that begins on the day that is 1 year before the date of bankruptcy and that ends on the date of bankruptcy, but no application for an order for relief is to be commenced by the trustee more than 1 year after the date of bankruptcy.

Comment: Subsection 24(3) responds to the fact that the trustee in bankruptcy of a bankrupt debtor may challenge transactions at undervalue and preferential transfers to creditors under both the *Bankruptcy and Insolvency Act* (*BIA*) and provincial law. The trustee may consider proceedings under this Act if relief is not available under federal law. Under the *BIA*, the trustee may challenge transactions that occurred within a period of time calculated from the date of bankruptcy and reaching back a specified number of months or years. The time that elapses after the date of bankruptcy before proceedings are commenced is not relevant. This enables the trustee to investigate the bankrupt's affairs, identify suspect transactions and take action. Subsection 24(3) allows the trustee to apply for relief under this Act in relation to a transaction that occurs within 1 year prior to the date of bankruptcy, giving him or her a similar opportunity to consider whether relief may be available under provincial law. Without such a rule, the limitation period might expire within days of the trustee's appointment and before any investigation has been made, thereby precluding relief. Unlike the *BIA*, subsection 24(3) imposes an end date on the period of time during which proceedings must be commenced by the trustee.

PART V Repeals

Statute of Fraudulent Conveyances repealed

25 The Act of the Parliament of England commonly called The Statute of Fraudulent Conveyances, being 13 Eliz. I, c. 5 (1571), is repealed to the extent that it applies to subject matters within the legislative jurisdiction of [*name of jurisdiction*].

[in jurisdictions where that Act is still in effect]

Repeal

26 [*insert name of relevant legislation*] is repealed.

APPENDIX B

Sample Draft Reviewable Transactions Act

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Reviewable Transactions Act

PART I
General

Definitions

1(1) In this Act,

"adult interdependent partner" means an adult interdependent partner as defined in the *Adult Interdependent Relationships Act*;

"claim" means the right to satisfaction of an obligation owed by a debtor, whether the obligation is

(a) liquidated or unliquidated,

(b) absolute or contingent,

(c) certain or disputed, or

(d) payable immediately or at a future time;

"confer" includes to create, grant, provide or transfer;

"creditor" means, subject to section 13, a person who holds a claim;

"creditor transaction" means a transaction under which a debtor directly or indirectly benefits a creditor by satisfying a claim in whole or in part or by providing security for the satisfaction of a claim in whole or in part but does not include

(a) a transaction under which a debtor

(i) satisfies an obligation that is secured by a security interest in property of the debtor to the extent that the security interest has priority over the rights of unsecured creditors of the debtor,

(ii) confers an interest in property as security for new value advanced by the transferee, or

(iii) gives a security interest in property in substitution for another security interest in property that is of equivalent value and that was given to secure the same obligation, or

(b) a transaction effected

(i) by obtaining or enforcing a court order, or

(ii) by operation of law;

"exempt property" means property that is exempt by law from seizure, attachment or any other measure to enforce a money judgment;

"insolvent", with respect to a person, means that

(a) the person is for any reason unable to meet his or her obligations as they generally become payable,

(b) the person has ceased paying his or her obligations in the ordinary course of business as they generally become payable, or

(c) the aggregate of the person's property, other than exempt property, is not, at a fair valuation, sufficient to enable payment of all his or her obligations, whether or not those obligations are currently payable;

"security interest" means an interest in property that secures payment or performance of an obligation and, in sections 3 and 4, includes an interest that is a security interest under section 1 of the *Personal Property Security Act*;

"separation agreement" means an agreement between a debtor and an individual who is or was the debtor's spouse or adult interdependent partner that

(a) results from or relates to the breakdown of the parties' relationship, and

(b) provides for the division of property and financial resources or for support for the individual who is or was the debtor's spouse or adult interdependent partner or for a member of the debtor's family;

"separation transaction" means a transaction in which the parties are or were spouses or adult interdependent partners and that is effected by

(a) a separation agreement, or

(b) a court order for the division of property and financial resources or for support resulting from the breakdown of the parties' relationship;

"spouse" means an individual who is married to another individual;

"transaction" means the conferral of a benefit and includes

(a) the conferral of an interest in existing property or property to be acquired in the future, whether or not the property is exempt property in the hands of the transferor, including a settlement on the transferor as a trustee under a trust,

(b) the provision of services,

(c) the payment of money,

(d) the release of an interest or obligation,

(e) the conferral of a security interest, charge, lien or encumbrance,

(f) the conferral of a licence, quota, right to use or right to payment,

(g) the designation of a beneficiary,

(h) the voluntary purchase or redemption of its shares by a corporation or the voluntary payment of a dividend by a corporation, other than a dividend in the form of its shares,

(i) the refusal by a debtor to act under a power of appointment to confer an interest in property on the debtor,

(j) the disclaimer of an interest in property, whether before or after the interest has vested,

(k) the creation or augmentation of a security interest held by a creditor in property of a debtor as a result of the satisfaction of an obligation owed to another person that is secured by a security interest in the same property if

(i) an unsecured claim of the creditor in that property becomes secured in whole or to a greater extent, or

(ii) a claim of the creditor in that property that was unsecured in part becomes secured in whole or to a greater extent,

(l) the satisfaction of an obligation owed by a person other the debtor,

(m) the conferral of a benefit by a court order or by operation of law;

(n) the assumption of an obligation to do or to bring about in the future any of the events or actions mentioned in clauses (a) to (m);

"transferee" means a person who benefits under a transaction and includes a creditor who benefits under a creditor transaction.

Applications for relief to be made to Court of Queen's Bench

2 All applications for an order for relief under this Act must be made to the Court of Queen's Bench.

Rights of secured creditors

3(1) A creditor whose claim is secured by a security interest in property of the debtor may apply for an order for relief under this Act but an order may be granted only with respect to the amount of the claim, if any, that exceeds the value of the property against which the security interest may be enforced

(2) If a debtor transfers property that is subject to a security interest and another Act provides that the security interest is subordinated to the interest of the transferee or that the transferee takes the property free of the security interest,

(a) the property is not to be considered property against which the security interest may be enforced for the purposes of subsection (1) in proceedings relating to that transfer or to another transaction; and

(b) if an order for relief is made under this Act in relation to the property transferred, whether in proceedings by the creditor or by another person, the creditor may not assert a claim to the property on the basis of the security interest.

Relief where transaction involves property subject to a security interest or writ of enforcement

4(1) An application for an order for relief may be made in relation to a transaction that involves property that is subject to a security interest or a writ of enforcement even if under another Act

(a) the security interest or the writ of enforcement is subordinated to the interest of the transferee; or

(b) the transferee takes the property free of the security interest or writ of enforcement.

(2) If a transaction involves property that is subject to a security interest at the date of the transaction, an order for relief may be made only if the transaction reduces the amount or value of property that would have been available to unsecured creditors under judgment enforcement measures if the transaction had not occurred.

(3) In determining under subsection (2) whether or not property would have been available to unsecured creditors under judgment enforcement measures if the transaction had not occurred,

(a) no regard is to be had to whether or not the property is or was exempt property; and

(b) if the security interest is subordinated to the interest of the transferee or the transferee takes free of the security interest, the security interest is to be considered unenforceable against unsecured creditors.

When applications for orders of relief may be made and claims may be established

5(1) An application for an order for relief under this Act may be made whether or not the person who applies for relief has commenced proceedings or obtained a judgment against the debtor in relation to a claim.

(2) A person who applies for an order for relief under this Act is entitled to a benefit under an order for relief only if a judgment has been granted against the debtor on the person's claim.

(3) If a person does not have a judgment against the debtor in relation to a claim,

(a) the person may make the debtor a defendant in the proceedings and the court may

(i) grant judgment against the debtor for the amount of the claim that is proven in the proceedings or that is not contested by the debtor, or

(ii) direct a separate trial to determine the validity and amount of the claim; and

(b) the court may

(i) stay the proceedings or suspend the operation of an order for relief until a judgment is obtained either as part of the proceedings related to the application for relief or in another action, and

(ii) make any supplementary orders that the court considers appropriate.

PART II
Transactions at Undervalue and Transactions Intended to Hinder or Defeat Creditors

Who may apply for order of relief under this Part

6(1) An application for an order for relief under this Part may be made by

(a) a person who holds a claim that existed at the date of the transaction that is the subject of the application for relief; and

(b) in the case of relief claimed on the grounds of relief mentioned in section 7(1)(b) or (c), a person who holds a claim that arose after the date of the transaction that is the subject of the application for relief.

(2) For the purposes of permitting an application for relief to be made under this section

(a) a person who has commenced legal proceedings seeking an interest in the property of a debtor or an order for the payment of money against a debtor is to be regarded as a person who holds a claim; and

(b) a person who is a defendant in the legal proceedings mentioned in clause (a) is to be regarded as a debtor whether or not a judgment has been granted against that person at the time the application is made.

Grounds for relief under this Part - transactions at undervalue or transactions intended to hinder or defeat creditors

7(1) Except as otherwise provided in this Act, an order for relief may be made under this Part

(a) in relation to a transaction in which the debtor receives no consideration or consideration worth conspicuously less than the value conferred by the debtor under the transaction, if the debtor

(i) is insolvent at the time of the transaction,

(ii) becomes insolvent as a result of the transaction, or

(iii) enters into the transaction in circumstances in which the debtor is demonstrably at risk of insolvency and the debtor becomes insolvent within 6 months after the date of the transaction;

(b) in relation to a transaction in which the debtor's primary intention is to hinder or defeat the right of a creditor or creditors to recover in whole or in part claims that, at the time of the transaction, were existing or were reasonably foreseeable, if

(i) the ability of the creditor or creditors to recover their claims is materially hindered as a result of the transaction, and

(ii) the debtor receives no consideration or consideration worth conspicuously less than the value conferred by the debtor under the transaction; or

(c) in relation to a transaction in which the debtor's primary intention is to hinder or defeat the right of a creditor or creditors to recover in whole or in part claims that, at the time of the transaction, were existing or were reasonably foreseeable, if

(i) the ability of the creditor or creditors to recover their claims is materially hindered as a result of the transaction, and

(ii) the transferee knew of the debtor's intention and intended to assist the debtor by entering into the transaction.

(2) For the purposes of subsection (1), if the transaction involves a corporation repurchasing or redeeming shares issued by the corporation, neither receipt of the shares by the corporation nor their surrender by the holder is to be regarded as consideration received by the corporation under the transaction.

(3) The court may consider the following factors, among others, in determining the intention of the debtor or the transferee:

(a) in the case of the debtor, whether the debtor was insolvent at the date of the transaction or became insolvent as a result of the transaction;

(b) in the case of the transferee, whether the transferee knew that the debtor was insolvent at the date of the transaction or would likely become insolvent as a result of the transaction;

(c) whether the transaction occurred at a time when the debtor or the transferee, as the case may be, knew of the existence of a claim against the debtor or had reasonable grounds to anticipate that a claim would arise in the foreseeable future;

(d) if the transaction was effected by a court order,

(i) in the case of the debtor, whether the debtor failed to disclose to the court in the proceedings under which that court order was made

(A) an existing or reasonably foreseeable claim that may be prejudiced by the order, or

(B) the extent of an existing or reasonably foreseeable claim, or

(ii) in the case of the transferee, whether the transferee failed to disclose to the court in the proceedings under which that court order was made

(A) an existing or reasonably foreseeable claim that may be prejudiced by the order and that was known to the transferee, or

(B) the extent of an existing or reasonably foreseeable claim that was known to the transferee;

(e) whether the value of the consideration received by the debtor was less than the value of the benefit conferred on the transferee;

(f) whether the parties to the transaction were related or closely affiliated;

(g) whether the debtor retained the possession, use or benefit of property or value transferred under the transaction;

(h) whether the transaction was entered into in haste;

(i) whether the debtor or the transferee attempted to keep the transaction or circumstances material to the availability of relief under this Act hidden from creditors or others;

(j) whether the transaction was not documented in the manner that would ordinarily be expected in relation to a transaction of that kind.

Relief in certain cases

8(1) In this section, "contingent obligation" means an obligation to pay money, transfer property or otherwise give value, the performance of which is contingent on an event that may or may not occur, and includes an obligation under a guarantee or an agreement to indemnify against loss occasioned by the default or non-performance of another person.

(2) An order for relief may be made in relation to the following transactions only if the grounds for relief mentioned in section 7(1)(c) are established:

(a) a separation transaction;

(b) a transaction involving the refusal by a debtor to act under a power of appointment to confer an interest in property on the debtor or the disclaimer of an interest in property before the interest has vested; or

(c) a transaction involving the assumption of a contingent obligation by the debtor.

(3) If a transaction, other than a separation transaction, is effected by a court order or by operation of law, an order for relief may be made only if the grounds for relief mentioned in section 7(1)(b) or (c) are established.

(4) If a transaction is effected by a court order, an order for relief may be made by any court having jurisdiction to grant relief under this Act, whether or not that court is the court that made the order effecting the transaction.

Transactions involving corporate payments

9(1) This section applies to a transaction that consists of the purchase or redemption of its shares by a debtor corporation or the declaration of dividends by a debtor corporation.

(2) If an order for relief is made against a shareholder as transferee in a transaction, the court may make an order for relief against a director or directors of the corporation, jointly and severally, to take effect if and to the extent that the order against the shareholder is not satisfied within 6 months after the date that the order is made.

(3) An order for relief must not be made under this section against

(a) a director who is not liable in relation to the actions constituting the transaction under any applicable Act or other law governing the corporation that provides for a remedy against a director in relation to a resolution or action authorizing the purchase or redemption of shares or the declaration of a dividend; or

(b) a director who had reasonable grounds to believe that the circumstances of the transaction were such that the transaction did not give rise to a remedy under the Act or law mentioned in clause (a).

(4) In determining whether a director had reasonable grounds within the meaning of subsection (3), the court must consider whether the director in good faith relied on, and whether a reasonable person in the director's position could be expected to rely on,

(a) financial statements of the corporation represented to the director by an officer of the corporation or in a written report of the auditor of the corporation to reflect fairly the financial condition of the corporation; or

(b) a report of a lawyer, accountant, engineer, appraiser or other person whose position or profession lends credibility to his or her statement.

(5) An order for relief must not be granted against a shareholder who, in proceedings taken under the *Canada Business Corporations Act* or the Alberta *Business Corporations Act* by the corporation or another person, has been ordered to restore to the corporation or to a director of the corporation any amount paid or the value of property distributed under the transaction.

(6) An order for relief must not be granted against a director who, in proceedings taken under the *Canada Business Corporations Act* or the Alberta *Business Corporations Act* by the corporation or another person, has been ordered

(a) to restore to the corporation any amount paid or the value of property distributed under the transaction; or

(b) to make a payment to satisfy a right of contribution held by another director who has been ordered to restore to the corporation any amount paid or the value of property distributed under the transaction.

(7) If an order for relief is made against a shareholder or a director in relation to a transaction,

(a) the order is not enforceable against that person if the person is subsequently ordered in proceedings under the *Canada Business Corporations Act* or under the Alberta *Business Corporations Act*

(i) to restore to the corporation an amount paid or the value of property distributed under the transaction, or

(ii) to satisfy an order for contribution; and

(b) the court may suspend enforcement of the order for relief until proceedings against that person under the *Canada*

Business Corporations Act or under the Alberta *Business Corporations Act* are concluded.

Orders for relief respecting creditor transactions

10(1) Subject to subsection (2), if a transaction is a creditor transaction, an order for relief may be made under this Part only to the extent that the value of the benefit conferred on the creditor exceeds the claim satisfied or secured by the creditor transaction.

(2) This Part applies to a separation transaction, whether or not the separation transaction is a creditor transaction in whole or in part.

Persons against whom relief may be granted under this Part

11(1) If grounds for relief mentioned in section 7 are established, the court may make an order for relief against either or both of the following:

(a) a transferee who received a benefit from the debtor under the transaction;

(b) subject to subsection (2), a person who has received all or part of the benefit conferred under the transaction from a person described in clause (a) or a subsequent transferee.

(2) An order for relief must not be made against a person mentioned in subsection (1)(b) if the person gave consideration that, in the opinion of the court, is worth not conspicuously less than the value of the benefit received and

(a) if the grounds for relief fall within section 7(1)(a), the person did not know that the benefit derived from a transaction that occurred in the circumstances described in that section; or

(b) if the grounds for relief fall within section 7(1)(b) or (c), the person did not know that the benefit derived from a transaction in which the debtor's primary intention was to hinder or defeat the enforcement of the rights of a creditor or creditors.

(3) If grounds for relief mentioned in section 9 are established, the court may make an order for relief against a director of a corporation.

PART III
Preferential Creditor Transactions

Who may apply for order of relief under this Part

12(1) Subject to subsection (2), an application for an order for relief under this Part may be made by a person who holds a claim that existed at the date of the creditor transaction that is the subject of the application for relief.

(2) If a claim is a right to satisfaction of an obligation that is contingent on a future uncertain event, the person who holds the claim may apply for relief only if, at the date of the creditor transaction that is the subject of the application for relief, it was reasonably foreseeable that the event would occur.

Grounds for relief under this Part - preferential creditor transactions

13(1) Except as otherwise provided in this Act, an order for relief may be made under this Part in relation to a creditor transaction if

(a) the creditor receiving the benefit conferred under the creditor transaction is not dealing at arm's length with the debtor; and

(b) the debtor

(i) is insolvent at the time of the creditor transaction,

(ii) becomes insolvent as a result of the creditor transaction, or

(iii) enters into the creditor transaction in circumstances in which the debtor is demonstrably at risk of insolvency and the debtor becomes insolvent within 6 months after the date of the creditor transaction.

(2) Persons who are related to each other are presumed not to deal with each other at arm's length while so related but the presumption may be rebutted by proof that they are dealing at arm's length.

(3) It is a question of fact whether persons not related to one another were at a particular time dealing with each other at arm's length.

(4) Persons are related to each other when they are related to each other for the purposes of the *Bankruptcy and Insolvency Act* (Canada).

(5) Persons are deemed to be dealing with each other at arm's length with respect to the following:

(a) a margin deposit made by a clearing member with a clearing house; or

(b) a transfer, charge or payment made in connection with financial collateral and in accordance with the provisions of an eligible financial contract.

(6) In this section,

"clearing house" means a body that acts as an intermediary for its clearing members in effecting securities transactions;

"clearing member" means a person engaged in the business of effecting securities transactions who uses a clearing house as intermediary;

"creditor" includes a surety or guarantor for the debt due to the creditor;

"financial collateral" and "eligible financial contract" have the meaning ascribed by the *Bankruptcy and Insolvency Act* (Canada);

"margin deposit" means a payment, deposit or transfer to a clearing house under the rules of the clearing house to assure the performance of the obligations of a clearing member in connection with security transactions, including, without limiting the generality of the foregoing, transactions respecting futures, options or other derivatives or to fulfil any of those obligations.

Non-application of Part to separation transactions

14 This Part does not apply to a separation transaction, notwithstanding that the separation transaction may be a creditor transaction in whole or in part.

Persons against whom relief may be granted under this Part

15 If grounds for relief under this Part are established, the court may make an order for relief against either or both of the following:

(a) the creditor receiving the benefit conferred under the creditor transaction;

(b) a person who has received all or part of the benefit conferred under the creditor transaction

(i) in a transaction with the creditor mentioned in clause (a), if the person was not dealing at arm's length with the creditor, or

(ii) in a transaction with a transferee who received all or part of the benefit from the creditor mentioned in clause (a) or a subsequent transferee, if the parties to each transaction leading to receipt of the benefit by the person against whom relief is claimed were not dealing at arm's length.

PART IV
Orders and Remedies

Nature of order under Part II

16 In granting relief under Part II, the court shall make any orders that it considers necessary to make available to the person who applies for relief the value conferred on the transferee under the transaction to the extent of that person's claim against the debtor, taking into account the provisions of section 18.

Nature of order under Part III

17(1) In granting relief under Part III, the court shall make any orders that it considers necessary to set aside the creditor transaction, taking into account the provisions of section 18.

(2) If an order for relief is made under Part III in relation to a creditor transaction that had the effect of discharging an obligation under a guarantee or indemnity or an obligation secured by a guarantee or indemnity, the obligation so discharged is revived to the extent that the payment is set aside, subject to any defences that the person who owes the obligation may otherwise be entitled to assert.

Forms of orders

18(1) In this section, "proceeds" means

(a) identifiable or traceable property that is derived directly or indirectly from any dealing with

(i) the property that is the subject of the transaction, or

(ii) the proceeds of the property that is the subject of the transaction; and

(b) the right to an insurance payment or any other payment as indemnity or compensation for loss of or damage to

(i) the property that is the subject of the transaction, or

(ii) the proceeds of property that is the subject of the transaction.

(2) In making an order for relief, the court may make an order or orders that may be required to achieve the result indicated in sections 16 and 17, including

(a) an order vesting in the debtor, or in another person, property that is the subject of the transaction or the proceeds of the property;

(b) an order declaring that property that is the subject of the transaction or the proceeds of that property be subject to judgment enforcement measures in the hands of the transferee;

(c) an order directing that property that is the subject of the transaction or the proceeds of the property be sold and the money realized on the sale distributed as the court may direct;

(d) an order requiring the transferee to pay a sum equivalent to the value of property or other benefits received under the transaction;

(e) except in the case of an order made under Part III, an order requiring the transferee to pay a sum in recognition of income earned through the use or exploitation of property or of a licence, quota, right to use or right to payment received under the transaction;

(f) an order directing the release or discharge of any debt incurred, or security or guarantee given, by the debtor under the transaction;

(g) an order reviving any obligation or security released by the debtor under the transaction;

(h) an order setting aside a designation in favour of a beneficiary;

(i) an order declaring that property that would otherwise be exempt as against creditors is subject to judgment enforcement measures;

(j) an order setting aside or varying a court order if the order constitutes a transaction giving rise to the entitlement to relief;

(k) an order appointing a receiver to take possession of and deal with property in the manner directed;

(l) an order granting an injunction against the debtor or another person.

(3) An order for relief must be made in those terms or subject to those conditions that the court considers necessary to make money payable or the value of property to be transferred under the order available for distribution to the persons qualified under the *Civil Enforcement Act* to share in the proceeds of judgment enforcement measures taken against the debtor.

(4) In making an order under subsection (3), the court may

(a) order that property owned by a person other than the debtor be sold in writ proceedings

(b) order that money paid by the transferee under the order for relief be paid to the clerk whereupon it shall be treated as a distributable fund in writ proceedings against the debtor, who shall be named, and distributed under Part 11 of the Civil Enforcement Act accordingly,

(c) order that, in the case of writ proceedings taken against the transferee to enforce an order for the payment of money, the funds generated by the proceedings shall be treated as a distributable fund in writ proceedings against the debtor, who shall be named, and distributed under Part 11 of the *Civil Enforcement Act* accordingly,

(d) make such other order as may be required.

(5) In granting relief under Part II,

(a) subject to subsection (6), the court may refuse an order or adjust the terms of an order, or make an order in favour of the transferee for recovery of an identified sum against the debtor, in recognition of the following:

(i) the value given by the transferee,

(ii) expenditures and non-monetary investments made by the transferee that have increased the value of property received by the transferee under the transaction, or that have generated income through the use of property or of a licence, quota, right to use or right to payment conferred by the debtor, to the extent of the expenditures made or the value invested,

(iii) actions taken by the transferee in reasonable reliance on the finality of the transaction under which a benefit was received; and

(b) if the court orders that property received by the transferee under a transaction or the proceeds of the property be vested in the debtor, the court may grant the transferee a security interest in the property that secures

(i) the value given by the transferee under the transaction, to the extent of that value, and

(ii) expenditures and non-monetary investments made by the transferee that have increased the value of the property, to the extent of the expenditures made or the value invested.

(6) The factors mentioned in subsection (5) are not to operate in favour of a transferee who knew that the debtor entered the transaction with the primary intention of hindering or defeating the enforcement of the rights of a creditor or creditors.

(7) In granting relief under Part III

(a) the court may, in recognition of expenditures and non-monetary investments made by the creditor that have increased the value of property received under the creditor transaction,

(i) adjust the terms of an order, or

(ii) make an order in favour of the creditor receiving the benefits conferred under the creditor transaction for recovery of an identified sum against the debtor; and

(b) if the court orders that property received by the creditor under the creditor transaction or its proceeds be vested in the debtor, the court may grant the creditor a security interest in the property securing expenditures and non-monetary investments made by the creditor that have increased the value of the property, to the extent of the expenditures made or the value invested.

Security interests created under order for relief

19(1) A security interest granted under section 18(5)(b)(i) has priority over the rights of creditors of the debtor that exist in relation to the property when the property vests in the debtor or that arise as a result of the vesting, other than rights associated with a perfected security interest that attached to the property before the transaction occurred.

(2) A security interest granted under section 18(5)(b)(ii) or 18(7)(b) has priority over the rights of all creditors of the debtor that exist in relation to the property when the property vests in the debtor or that arise as a result of the vesting, including the rights of secured creditors.

(3) A security interest in property granted under sections 18(5) or 18(7) may be registered

(a) in the Personal Property Registry if the property is personal property, or

(b) in the Land Titles registry if the property is land.

(4) Subject to subsections (1) and (2), a security interest granted under section 18(5) or (7)

(a) that is registered in the Personal Property Registry under subsection (3)(a) has the status of a security interest perfected by registration under the *Personal Property Security Act*, or

(b) that is registered in the Land Titles registry under subsection (3)(b) has the status of an interest in land registered under the *Land Titles Act*

Application of orders for relief to exempt property

20(1) If an order for relief is granted in relation to a transaction involving exempt property and the debtor continues to use the property in the manner that attracted the exemption, the court

(a) may suspend enforcement of the order for relief until the time that the debtor ceases to use the property in that manner; and

(b) if the enforcement of an order for relief is suspended under clause (a), may grant an attachment order against the transferee.

(2) An attachment order granted under subsection (1)(b):

(a) shall direct that the order applies to the exempt property;

(b) may prohibit any dealing with the property or may impose conditions or restrictions on any dealings with the property that may be required to preserve it for purposes of enforcement of the order for relief at the time referred to in subsection (1)(a);

(c) may be registered as provided in section 22 of the *Civil Enforcement Act*;

(d) upon registration under clause (c), has the priority status prescribed in relation to an attachment order by section 23(1) of the *Civil Enforcement Act*.

(3) The provisions of the *Civil Enforcement Act* applicable to attachment orders do not apply to an attachment order granted under this Act, with the exception of sections 17(3)(g) and 17(8) of the *Civil Enforcement Act* and the provisions of the *Civil Enforcement Act* indicated in subsection (2).

Application of Part to subsequent transferees and creditors

21 This Part applies, with any necessary modification, to an order for relief made against a person mentioned in section 11(1)(b) or 15(b).

Order for relief in relation to corporate transactions

22(1) If an application for relief is made in relation to a transaction mentioned in section 9(1), sections 9(2) to (7) must be taken into account in the making or refusal of an order for relief.

(2) If an order for relief is made against a director under section 9, the order must require the director to pay a sum of money equivalent to the amount paid by the corporation under the transaction, and the provisions of this Part, other than sections 18(3), 23 and 24, do not apply.

Injunctions and attachment orders

23(1) Whether or not an application for an order for relief has been made, the court may grant an injunction, an attachment order or both to a person who is, or who may become, entitled to apply for an order for relief under this Act if the court is satisfied that there is a reasonable likelihood that a transaction giving rise to a right to relief has occurred or is about to occur.

(2) In granting an injunction, the court may make any orders against the debtor or another person that the court considers necessary to

(a) preserve the benefit of any final order for relief that may be granted;

(b) allow an appropriate order for relief to be made; or

(c) prevent a transaction from occurring.

(3) An attachment order referred to in subsection (1) may be granted against the debtor or another person.

(4) The provisions of the *Civil Enforcement Act* that apply to an attachment order apply to an attachment order granted under this section.

Limitation of actions

24(1) Subject to subsections (2) and (3), no application for an order for relief is to be commenced more than 1 year after the date of a transaction.

(2) If the transferee conceals or assists in the concealment of the transaction that is the subject of the application for relief or of facts

material to the grounds for relief, the 1-year period mentioned in subsection (1) commences at the time that the person making the application knew of the transaction or the material facts, but no application for relief is to be commenced more than 5 years from the date of the transaction.

(3) If the debtor becomes bankrupt before the end of the 1-year period mentioned in subsection (1), the debtor's trustee in bankruptcy may bring an application for an order for relief if the transaction that is the subject of the application for relief occurred during the period that begins on the day that is 1 year before the date of bankruptcy and that ends on the date of bankruptcy, but no application for an order for relief is to be commenced by the trustee more than 1 year after the date of bankruptcy.

PART V Repeals

Statute of Fraudulent Conveyances does not apply

25 The *Statute of Fraudulent Conveyances, 1571*, 13 Eliz. I, c. 5 does not apply to Alberta with respect to matters within the legislative authority of Alberta.

Repeal

26 [*insert name of relevant legislation*] is repealed.